Economic Affairs / A Monthly Analysis

A special supplement to CHALLENGE

February 1, 1961

UNCERTAINTY is the current key word. The semantic arguments are over, and it's officially a recession. Hindsight tells us that it began in the middle of last year, when the indicators hit their peaks. The question now is: How long and how deep a recession are we in for?

Of the 4 basic expenditures that make up gross national product, 2 are falling and 2 are rising. Together they add up to a net decline.

Consumer expenditures fell from an annual rate of $329 billion to $328.3 billion during the third quarter of 1960. And that was while personal income was still rising. Now, personal income is leveling off, and consumers are tightening their purse strings. Uncertainty about layoffs and shorter hours makes them more prudent. The 4.4 million persons who are unemployed are, of course, in no position to step up their purchases.

Businessmen are more prudent, too. They're still cutting down on inventories and planning smaller outlays for equipment. In 1960 investment in plant and equipment amounted to $35.7 billion. During the first quarter of 1961 it is expected to drop to a $34.9 billion annual rate, and less than that in the second quarter.

Net exports are rising. Europe is still buying from us and our imports from abroad are low. But with the European boom showing signs of getting tired, there's the possibility that our foreign sales may fall off.

Government spending is rising. It was up to an annual rate of $100.7 billion during the third quarter of 1960, and keeps climbing. What's not so certain as yet is: How much higher will it go and where will the funds be spent?

There's uncertainty on the monetary side, too. Higher government spending and lower tax collections require considerable deficit financing. The Federal Reserve's dilemma is that lower interest rates will step up the gold outflow, while higher ones will slow our recovery. Unless the Fed eases money further, the increased supply of government bonds will drive bond prices down—and interest rates up.

The new Administration will be making its plans known quickly. Depressed areas, extension of unemployment insurance and housing are likely to get earliest attention. Tax changes are also being talked of.

In the midst of all this it is important to remember that, in addition to the current recession, we have a longer-run problem. Resources have to be shifted out of sectors where demand is no longer brisk—such as consumer durables and suburban middle-income housing—and into the rising service industries. The European economy is rebuilt and our export industries must find new products where our advantage is greatest.

Automation must be introduced without too many dislocations. The process of recovery from this recession will be aided by adjustments to these problems.

SPECIAL CORRESPONDENCE—Biggest domestic headache facing the Kennedy Administration is the deepening recession. Most economists are now very pessimistic about a quick recovery. Federal efforts to combat the downturn may have to be more extensive than anything anticipated at the time of the election.

Current estimates of a budget deficit for fiscal 1962 of up to $6 billion are conservative. There's a good chance that the deficit will top $10 billion.

Fiscal responsibility, as personified in the appointment of Douglas Dillon as Treasury Secretary, will not help much to avoid a deficit any more than a $12-billion deficit could be avoided in 1959 under Secretary Anderson.

Receipts by the government have been particularly hard-hit, thus leaving the Treasury pressed for money at a time when the outgo is bound to increase. Raising taxes is out of the question. Consumer expenditures, as well as capital expenditures, are already in the doldrums. In fact, very few changes in the tax structure can be expected in this session of Congress. The job is too big for quick measures, and the oft-spoken of flexible tax rates will be put off for future consideration.

The Kennedy Administration is confronted with basic economic problems that have been developing for the past 15 years. Pre-World War II consumption patterns are now considerably altered. Industries which were formerly considered bellwethers of the economy—like steel and autos—can no longer expect to maintain their phenomenal postwar growth. Shifts in the pattern of capital investment are also in the offing.

All this is leading to serious dislocations as the decade of the Sixties unfolds. Employment needs are changing. The technological revolution is placing a different emphasis on skills. New depressed areas appear as industries and markets change. A renewed matching of supply with demand awaits a more complete analysis of what people really want to buy and how much they are willing to spend.

Problems like these will not shake themselves out in a matter of months. A long-term process of readjustment is now anticipated by the Kennedy people. Another consumer spree will not occur until 1964, according to most informed estimates.

In only one respect does the recession make the new President's job easier. Many of his remedial bills, like aid to depressed areas, if they are conservatively drawn, will have clear sailing. Some kind of assistance to the aged to pay medical bills is in the offing, as is additional federal help in the financing of low- and middle-income housing.

The balance of payments problem has caught up with Britain as well as the U.S.A., both of whom also must step up their rates of economic growth. In the case of the British, however, the problem can be traced almost wholly to continuing trade deficits—more than $500 million for the second half of 1960. Many of Britain's exports, plagued by high costs, have priced themselves out of world markets.

The nations of Europe, particularly those in the Common Market, are moving forward vigorously. They have no balance of payments problem. Productivity increases continue to offset wage increases, while crumbling tariff walls have exposed a huge market potential.

In the meantime, the Germans are having their problems with warding off requests from the United States that more German money go into underdeveloped areas. The British have also stepped in, asking for a stepped up program of sales of British arms to help with their balance of payments. The Germans would prefer an all-European solution, with some kind of a bridge between the Common Market and the Outer Seven.

Challenge

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Editorial

THE TURNING POINT

THE YEAR 1945 marked the most significant turning point in the modern history of the world. We have only just begun to grasp this fact, and I imagine that as John Kennedy took his oath of office as 35th President the implications of this realization must have occupied a greater part of his mind than even the domestic concern over recession, depressed areas and medical aid for the aged. For as unpalatable a thought as it may seem to most Americans who are accustomed to thinking of their nation as a sanctuary against the din and foibles of the rest of the world, the constant intrusion of events abroad since the end of World War II has become the inescapable component of the hopes and aspirations of the smallest political ward in this country.

For 15 years the United States has witnessed a series of international disturbances. We have put labels on these disturbances, calling them the problems of postwar reconstruction, the spawns of the cold war, the aspirations of underdeveloped economies, the yearnings for freedom, and so on. At best such labels truthfully express a generalization; at worst they becloud the essential nature of what in greater truth is a world-wide revolution.

In retrospect, it appears that our appraisal of this world-wide revolution was considerably hindered by an underestimation of how much of a break with the past occurred in 1945. Wars had always brought changes, but there was no precedent for the exhaustive shake-up that has been in progress since the end of World War II. This departure from precedent put a premium on adroitness and pragmatism in a way that challenged the creative instincts of policy makers. The challenge has not been met as well as it might have.

In one significant respect the arch opportunists of the Communist world were better suited than we to take advantage of the cutoff from the past. As revolutionaries themselves, contemptuous of gradualism and orderly transition, disrespectful of precedent and eager to reduce to raw putty that which they would reshape into their own image, they could rush into every situation of despair, hope for betterment and impatience. The turning point of 1945 was the beginning of a new era for the Communist revolutionaries. For us it was the end of a chapter which had never been conceived as requiring a spirited follow-up.

Of all the factors in the forementioned world revolution which have served to put the West at a disadvantage, the most serious has been colonialism of the type practiced by the maritime, commercial powers of Europe. The vestigial remains of policies that seemed appropriate and necessary in the 18th and 19th centuries now haunt the postwar structure of our society.

It is the American misfortune to fall heir to episodes in the history of allies. Even defensive measures taken in our own hemisphere have become open to misinterpretation by peoples who need a scapegoat for their own difficulties. It is not worth much to point out, in turn, the pattern of Eastern imperialism; for there the job has been more thoroughly done by the imperialists, leaving few voices who might dare to speak the truth.

Whether we like it or not, whether justified or not, anticolonialism has become the rallying cry of people eager for a change—in Southeast Asia, the Middle East, Africa and in Latin America. There is no use complaining or even explaining that the colonialism of the Western powers cannot and should not be held solely responsible, even where it existed, for such large reservoirs of poverty. The point is that everywhere except in Latin America (where the problem has not been colonialism for a long time but rather a kind of social somnambulism left undisturbed by its own privileged classes), the Western powers have been reluctant to respond to the revolutionary ambitions of former colonies and overseas territories. Nor does it help the Western cause to find Belgians rioting in the streets of Brussels because of economic losses sustained from the independence of the Congo, a circumstance that deflates the original contention that the Congo was not ready for self-rule.

In short, there is a world movement afoot, which for better or for worse is carrying us along at a faster pace than anything we could have imagined possible 15 years ago. Material progress is the order of the day, and that kind of progress there will be, with or without orderly process. It now falls to the United States to recognize that the difference between materialistic nihilism and a stable world where established men of good will can help their neighbors is the difference between nostalgia and the fearless facing up to new world forces.

point of no return

The time has come to display a special adroitness of our own, the kind that others refer to as Yankee ingenuity. If people everywhere want to live better, we are for it. It is assumed in most parts of the world that Americans have a monopoly on good living. As teachers of how to do it, we should have no peers. If we go at this with conviction, Western civilization can put into proper historical perspective its era of colonialism.

We can ill afford indiscretions or disingenuous arguments. Either we are worthy of our predecessors or we are not. The world has broken with the past. Its future is in our hands. If we do not display the proper dexterity now, our expectations for higher living standards at home for all of our own people will be as fruitless as an apple orchard in the Antarctic.—H. B.

LETTERS TO THE EDITOR

CHALLENGE invites your comments. Address letters to CHALLENGE, 475 Fifth Avenue, New York 17, N. Y.

UNFAIR TAXES

• The splendid article "The Invisible Hand of Tax Exemption," by Norman B. Ture, in your November issue, has received my heartiest approval. I am sending it to my senator at once.

If we are to have taxes—and there is some disagreement among millions of Americans as to why we should have them at all, except locally—then indeed, as Mr. Ture has brought out so cogently, they should be more fair. I am a novelist, and so I speak for all the other self-employed, small businessmen, doctors, lawyers, etc. We have no pensions, no fringe benefits, no sick and dependents' insurance, no companies to pay for lavish entertainments and stand the dozens of other expenses Mr. Ture mentions, no retirement incomes, no security whatsoever. This is particularly true of writers, who can never tell, from one year to another, whether they'll have any income at all, or if they are doomed to die of starvation in their old age. Each book is an enormous gamble, after years of the most concentrated and torturous work, isolation, blood, sweat and tears, research and pain, and hope and despair. We never know, until after publication, whether we've produced a best seller (and if so, the royalties go heavily to taxes) or if the book will die on the counters. Each book is an entirely new venture; you start from scratch, no matter how well known you are.

Writers, too, have families and obligations. (At one time we had eight dependents, for instance.) If we become sick and disabled, our income stops immediately, without the cushions of unemployment insurance and health insurance, and what not. A long illness is an enormous calamity. My husband, who is my collaborator, had a terrible operation one October, which was immediately followed by a major operation on my daughter, and directly after that I had a major operation. We had to take out a loan to pay medical and other expenses—though that year had been one of our most prosperous. You see, the greater part of our income had gone to federal and state taxes.

Writers, too, have to travel for local color and publicity. These are paid for by the writers, and each miserable item is scrutinized by the tax collectors, a torment not suffered by executives on expense accounts paid by their companies. We work without income for many years, while writing books. For instance, we worked on one book from 1926 to 1934, and then we worked on it again for another three years, 11 years in all. Unfortunately, when it was finally published it became a great best seller, was sold to the movies and was serialized. After we had paid federal and state income taxes, as on a daily wage, we discovered that we had been working for $400 apiece for each of those 11 years! Naturally, we had no savings. We had reached just about the highest bracket. No one prospered from that book but the government.

We still have best sellers. We haven't saved a dime since 1947. I am 60, my husband is 72. I am chronically ill, now, and each day's work becomes more and more unbearable. In fact, I am over 60 per cent disabled. And we have nothing to show for all our years of work, as best-selling writers, but a mortgaged house and a five-year-old car, and a fur coat 18 years old. An executive receiving the very same income would be independently rich now, and retired. We can't afford to retire. We still work up to 18 hours a day.

This is true, from what I have heard personally, of all other writers, and doctors and lawyers, and independent small businessmen and other self-employed people. This is disastrously unfair. It is, in the case of doctors, dangerous. I know many physicians who will take only a limited number of patients, in order to keep in a lower tax bracket. They refuse to go out on night calls. I know a famous Hollywood actor who refused to appear in a large picture because the money he would have received after taxes would have left him not even enough money to live on for three months. Accordingly, 2,000 people who would have been employed in that picture remained unemployed. Once you get into a high tax bracket you receive a smaller income, something which others do not seem to understand. It is easier to aim for the smaller income, and so others suffer in a widening circle, such as charities. One "small" businessman I know could expand and employ at least 50 more people. He refuses to do so. His income would rise rapidly—and so would his taxes and his responsibilities. So, he keeps his company, and his income, within strict bounds, and he keeps his health and peace of mind. And 50 people are jobless.

No one listens to the wretched taxpayer, of course. But I think taxes should be levied—if they are levied at all—on a straight, across-the-board basis: the first $2,000 of income totally exempt, and all income above that taxed 25 per cent, and with progressive rates eliminated. There should be no deductions for anything or anyone whatsoever. And, after the age of 60, no one should pay taxes at all. What few years are left should be spent in the saving of money for imminent old age and illness and loss of future income. As for the self-employed, who have no pensions and other fringe benefits, they should be permitted to invest, in annuities or good stock, a certain reasonable amount tax-free, to make up for the inequity. This would benefit industry, too.

Some economist has worked all this out, and has discovered that the federal government, under such a system, would have far more receipts than it does now! Best of all, faith in a just government would be restored, a faith that no longer exists. This, of course, is calamitous for the nation.

TAYLOR CALDWELL

Buffalo, N.Y.

AID TO UNDERSTANDING

• Thank you for the little square gimmick you used to summarize The Inner Six and the Outer Seven ("At Sixes and Sevens," November, 1960). Those of us who want to get the countries in the various organizations straight were helped immeasurably.

CLAIRE J. LANDAU

New York, N.Y.

WAGING THE COLD WAR

• I heartily agree with Mr. Raskin when he says that our unused manpower and industrial might need to be used to bring greater prosperity to all the people of the world ("How to Deflate the Labor Force," December, 1960). This is one of the greatest problems of the cold war, and it cannot be solved by an unimaginative "business as usual" approach.

A. N. ROBINSON

Buffalo, N.Y.

WELL RECEIVED

• Congratulations on your new magazine [format]. I hope it is well received by your other subscribers.

HARRY JAMEISON

Madison, N.J.

Challenge
THE MAGAZINE OF ECONOMIC AFFAIRS
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THE POLITICS OF TAX REFORM

by ROBERT METZ

■ TAXES ARE ALL-PERVADING. They fill the air like smog, blurring vision and making breathing difficult. And yet, they are vital to civilized life, providing the means to finance it, while serving as a device for shaping it that is as useful as it is unpredictable.

The new Congress will wrestle with taxes as spiritedly as with anything else, and will make changes in the law that will affect most of us. However, tax law changes do not come easily, or, in some instances, even rationally. Further, many of the legislative techniques used in bringing about tax law changes are quite distinguishable from those used for general legislation.

Just how difficult it is to make changes—especially basic changes—may be illustrated. For more than a year now, the House Ways and Means Committee has been studying the tax law as a prelude to major reform legislation. The Committee's chairman, Wilbur D. Mills (D.-Ark.), a highly respected tax authority, has predicted that several sessions will pass before the many proposals already submitted to the Committee have been studied, digested and drafted into bills.

General tax reform seems always to be on the agenda of the Ways and Means Committee. In 1954 a major reform was actually accomplished. But most students of taxation believe the 1954 reform failed to come to grips with the basic problem—erosion of the tax base.

The nominal personal income tax rates rise from 20 per cent to 91 per cent, and yet the wealthy pay at an estimated average rate of about 36 per cent. This is largely because congressmen believe the rates are too high and thus they have been willing to allow changes in the law that blunt the effect of the high rates.

Income has been converted into capital gains in certain situations, for a top tax rate of 25 per cent. Investments can be made in tax-free municipal bonds or in oil wells with tax concessions for depletion of resources. Further, the lower rates paid by corporations encourage individuals to incorporate themselves, thereby adding to the distortions of the tax law.

A good general tax reform would lower the top personal tax rates to acceptable levels—probably in line with the 52 per cent top corporate tax rate—and it would tighten the rest of the law, including capital gains provisions, and severely restrict oil depletion allowances, the base of many immense personal fortunes. Many other changes would, of course, be necessary to clean up the basic law, but these would probably be a necessary beginning to a true reform.

Prospects for basic reform

What are the chances for a basic reform? One specialist close to the Ways and Means Committee has said there is no prospect whatever of an over-all reform in the next several Congresses.

A tax expert summarized the feeling of most political realists when he said recently, "I'm skeptical about a broad-scale tax reform—ever. Too much give and take is involved." Other tax specialists don't want reform, and rely on the maxim, "Old laws are good laws," which might be more accurately stated, "Complicated laws are lucrative laws."

Meanwhile, dozens of tax proposals aimed at changing specific areas of the law will be revived during the coming session, or proposed for the first time. But little in the way of new tax legislation that is proposed from the floor of Congress is likely to command the respectful attention of the membership for some time. The primary reason for this is that during the initial "honeymoon" days of the new Administration, President Kennedy will propose much important legislation that will consume the energies of Congress.

Rather than pressing for legislation on its own, the House Ways and Means Committee will look to the White House for direction until such important fields for legislation as area redevelopment, unemployment and the flagging highway program are out of the way.

It is likely that the new President will sponsor a tax bill or two of his own. A social-security-tax-financed medical aid to the aged bill will be an early candidate for enactment. While this bill foundered in the 86th Congress last August, with the authority of the Presidency behind it and a more or less friendly Congress in the capable hands of Vice President Lyndon B. Johnson, the aid for the aged bill's chances of success early in this session are greatly enhanced.

With the lengthening shadow of recession darkening the scene, the new President may well use taxes as an important tool in his attempts to reverse the economic trend. Perhaps the President will seek tax forgiveness to stimulate consumption and thereby spark production.

Labor has already announced that it will press for a two-months tax forgiveness bill in view of the fact that 5.5 to six million workers are expected to be unemployed by the time this article appears. The tax forgiveness proposal would relieve taxpayers of a collective obligation estimated at $2.5 billion a month.

However, such a program undoubtedly would carry with it a

program of national deficit financing. Tight-fisted Sen. Harry F. Byrd (D.-Va.), who withheld his political support from Sen. Kennedy during the election campaign and who was a rallying force for Southern Conservatives then, expressed his opposition to tax forgiveness the day labor proposed it.

Since a tax forgiveness bill must have the endorsement of the Senate Finance Committee, of which Sen. Byrd is chairman, its passage is out of the question, no matter how much rank-and-file support it has in Congress.

The tax ax

But while any tax concession will cost money, at least initially, tax concessions there will be. Almost certainly, the next Congress will pass some form of legislation that will permit businessmen to protect some of their income dollars from the "take-half" tax ax by allowing them to charge as expenses a larger portion of the cost of their machinery each year.

If we can divide tax bills into the controversial—those that inspire political debate—and the noncontroversial—those proposed by lawyers and accountants to close widely recognized loopholes, the liberalized depreciation proposal is definitely in the controversial class.

What are the forces in favor of this measure?

Both political parties put planks in their platforms declaring in favor of liberalized depreciation allowances. President Kennedy said during the campaign, "Wherever we can be certain that tax revision, including accelerated depreciation, will encourage modernization of our capital plant—and not be a disguise for tax avoidance—we should proceed with such revision."

Of some $300 billion worth of machinery in the United States' industrial plant, some $95 billion worth is obsolete. Meanwhile, our competitors for world markets, Western Europe and Japan in the East, have modern industrial machines built from the ground up after World War II—mostly with American aid money. Their depreciation allowances invariably are more liberal than our own.

The increasing competition for our own markets domestically and abroad is part of the reason for the present unfavorable balance of trade. This unfavorable balance is dramatically illustrated by a gold outflow of over $4.5 billion since the beginning of 1958.

Foreign imports, always a challenge to American manufacturers due to our relatively high labor costs, become even more challenging when they are produced on machines newer than our own.

Basically, the problem is that business here is required to depreciate machinery over excessively long periods in order to get full tax benefits. Many types of textile machinery, for example, generally are depreciated over a 15-year period, while the machines' useful lives may last for as few as five years.

Reform legislation could streamline these antiquated useful-life rules, trimming the depreciation

periods to a more reasonable level.

There have been moves to liberalize depreciation allowances in recent years. Taking another approach to the problem in 1954, the law was changed so that businessmen could take top-heavy allowances during the early years of a machine's existence. But this has resulted in a brisk market in fairly new equipment. When this equipment is sold at a profit, the profit has been taxed at 25 per cent capital gains rates rather than the 52 per cent ordinary income rate.

The Treasury has just surveyed 6,000 businessess to find out what they think of present depreciation allowances. The survey is being evaluated now, and preliminary indications are that most businesses would be willing to give up the tax profits in used equipment sales for more adequate depreciation allowances.

Meanwhile, organized labor is on record as opposed to the faster depreciation methods put in the law in 1954. The AFL-CIO research department has even argued that it is not adequately proven that business needs better incentives for capital investment.

But it is quite likely that this position is the instinctive response to measures favoring business that could be subject to abuse. In that depreciation reform has so much momentum, and in that it must seem reasonable even to labor that a reform would improve the nation's competitive position relative to Western Europe and Japan, it is unlikely that labor will lobby strongly against a reform bill. Labor is increasingly concerned about low-cost foreign imports and their effect on job availability.

Legislative factors must also be weighed. Rep. Eugene J. Keogh (D.-Bklyn.), sponsored a bill for liberalizing depreciation allowances during the last session of Congress. Since the new President has indicated that he will deal with office-holders from powerful New York State rather than with political bosses, it is likely that Rep. Keogh will be a strong figure in the new Administration.

Encouraging support

Here is another legislative straw in the wind favoring a depreciation reform bill. Sen. Harrison A. Williams, Jr. (D.-N.J.), has announced that he will sponsor legislation to liberalize depreciation allowances during the next session. Support from liberals like Williams must certainly be encouraging to proponents of reforms to the law on depreciation.

Needless to say, strong support of the idea by President Kennedy would help immeasurably to put a reform bill over. He is likely to fight for it because it is a reasonably sure method of stimulating plant investment during recession years.

Thus, with the many factors working toward the passage of a liberalized depreciation law, it can be said with some certainty that a bill will be passed next session. As to the form of the bill, the willingness of businessmen to give up the tax profits from the sale of used equipment will assure the loss of capital gains treatment of such profits in the future. Thus, new legislation will either further liberalize the amount that can be deducted for depreciation in the early years or it will shorten the prescribed useful lifetime of machinery. Since the useful life concept is so far out of date at present, and in view of labor's opposition to top-heavy early year depreciation, it is reasonable to assume that Congress will move to make faster depreciation possible.

But who is to determine the useful life of the multitude of types of equipment in a variety of uses? A bill introduced during the last session of Congress would have left this tedious and unrewarding task to the Secretary of the Treasury. This is probably too much to ask of the Secretary in that it involves many seemingly arbitrary decisions.

There is already considerable sentiment for adopting the rules governing useful lives used by Canada —roughly half those prevailing here. It seems likely that Congress will fasten on this ready-made scheme to change our useful-life rules. The Canadian formula was set up by an independent commission.

Changed political outlook

Just how irrational the business of changing the tax laws can be is illustrated by the changed political outlook for any law proposed to alter the rules on oil depletion allowances.

When Sen. Kennedy debated oil depletion allowances with Vice President Nixon in the third television debate, he said he favored a thorough study of depletion allowances on all minerals to see if loopholes existed. He noted that he had once voted to reduce the 27.5 per cent depletion allowance for the largest oil producers.

A *Fortune* magazine study in November, 1957, resulted in a list of 50 of the wealthiest individuals in the nation and showed that more than 20 of these based their wealth on oil. Some had inherited their oil wealth; and some won it themselves. Undoubtedly, the liberal depletion allowances contributed to the wealth of many of the latter.

A man who owns a producing oil well pays taxes on only 72.5 per cent of the gross income of his well, so long as he pays a tax on at least 50 per cent of his taxable income. Depletion allowances were set up because oil drillers sink many wells that prove dry, and many producing wells peter out before returning on the investment in them.

Role of the Treasury

Many people both in and out of Congress believe depletion allowances for oil are far too liberal and constitute a loophole. And yet, the political realists assert the subject was removed from consideration as a live issue when Sen. Lyndon B. Johnson, of oil-rich Texas, became Sen. Kennedy's running mate. Still, the subject will undoubtedly come up, if only to embarrass the Democrats.

Any discussion of tax legislation would be incomplete without mention of the role the Treasury plays in the drama. Always pressed for funds to support the nation's $80-billion annual budget, the Treasury must constantly look for new ways to raise money. And it must make sure present laws are efficiently administered. Thus, the Treasury is often the behind-the-scenes proponent of legislation designed to raise tax revenues and is the only consistent bulwark against the congressman's "little ole tax amendment." This is Harvard Prof. Stanley Surrey's term for a tax change introduced in favor of a small group of deserving taxpayers. He points out that the Treasury knows it must be alert that these pinpricks in the tax law fabric don't become large holes through interpretations that funnel out hundreds of millions in tax revenues.

As the major opposition to revenue-curtailing tax law changes, the Treasury occupies a unique role in the U.S. legislative process. Consider almost any other important area for legislation—civil rights, schools, business, to name a few—and there are vocal groups outside the government fighting to maintain the status quo. Not so in the case of taxes. Everybody wants a smaller tax bill, and the collective response of taxpayers generally to this aspiration is sympathetic.

One way in which the Treasury has been active recently in attempting to protect the productivity of the tax laws is in getting taxpayers to report interest and dividend income. An estimated $3 billion in interest income and $1.5 billion of dividend income was not being reported each year in late 1959 when the Treasury began its educational campaign to get taxpayers to report this income. About $500 million in revenues was lost as a result of this failure to report the income.

Recently, at the Treasury's behest, banks and corporations have been notifying depositors and stockholders that the income is taxable. Late in December the Treasury said it was pleased with the results of its campaign. While once in favor of laws that would allow withholding on dividends and interest income, the Treasury would now like to avoid such legislation. Instead it wants a bill that will augment its efforts to automate tax collection. The idea is to assign taxpayers account numbers keyed to the social security numbering designations and then track down unreported income through the data processing machines that are gradually being installed in the Treasury. Banks and corporations would supply the raw material in the form of punched cards showing who received interest and dividend payments.

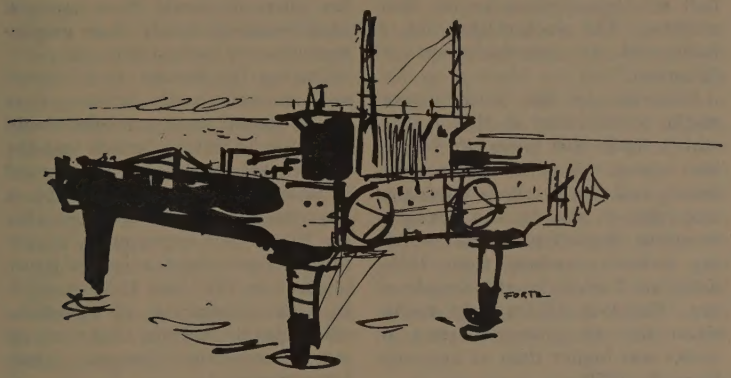
Congressional sentiment

Still, there is considerable Congressional sentiment for withholding on this income, and the key to legislation of this type is President Kennedy. During the campaign he indicated he favored withholding to close the dividend and interest income tax gap. However, the imminence of data processing and the fact that many people of low income depend on interest and dividend income to augment meager funds for living expenses makes it unlikely that this law will be enacted.

President Kennedy has already shown considerable interest in finding the most efficient means of ac-

complishing a result, and it is unlikely that the modest political rewards in a dividend-interest withholding law will commend it to his attention, since the problem can be solved through data processing methods.

Another revenue loss that has been a matter of particular concern to the Treasury results from a widely recognized abuse of expense accounts. The possibility of a hard law to stop this abuse will have a deleterious effect on a cherished piece of legislation that business has been seeking for some time—the right to deduct lobbying costs as a business expense.



Moral suasion

The Treasury has been conducting a campaign of moral suasion and a crackdown on the deduction of yacht, hunting lodge and hotel suite expenses in an effort to get business to eliminate expense account abuses without legislation. It is now evaluating its efforts.

While the complete results of its efforts will not be ready until 1962, initial information will be available soon. Meanwhile, another study is under preparation by Colin Stam, the highly respected head of the research staff of the Joint Congressional Committee on Internal Revenue Taxation. He has indicated that he will not wait for the final information on the Treasury study to submit his own report.

One man close to the Ways and Means Committee, and to Congress generally, said that Congress is pretty much of the opinion that it wants legislation to cut out the abuses. "Human nature being what it is, it is unlikely that reform will take place without legislation," he said. The fact that the nation is in a recession makes it a time for sacrifice, especially in view of our deteriorating economy *vis-à-vis* the rest of the world. Thus, Congress will probably jump in and legislate away the luxury-living aspects of expense accounts.

As to the form such legislation is likely to take, the best prospect is a bill introduced last year by influential Pennsylvania Sen. Joseph S. Clark, Jr. He wants to bar any deductions for entertainment expenses other than those for food or beverages. Business gifts of over $10 a person and dues or initiation fees in social, athletic or sporting clubs or organizations would also be ruled out. This proposal was killed in a House-Senate conference last year, but only after the conferees decided to give the Treasury another chance to control expense deductions by administrative means.

As to the lobbying bill, which is sponsored by Hale Boggs (D.-La.), and a member of the House Ways and Means Committee, many congressmen are willing to go along with it, despite a 40-year precedent against permitting such a deduction. Congress concedes privately that much of what business does in the way of lobbying is not mere cajolery, but well-considered and reasoned argument in favor of legitimate positions.

Two things will sound the death knell on this bill during the coming session. It is recognized that most of these expenses are deducted now, one way or another, and a bill legalizing the deduction is thus not very pressing. Furthermore, the bill that will be aimed at stopping expense account abuses will mobilize a heavy body of opinion for tightening rules, and this will weigh against the passage of a bill that goes in the opposite direction.

In the realm of noncontroversial legislation are several provisions designed to close revenue leaks opened by Congress inadvertently during the drafting of the 1954 tax-law reform legislation. The passage into law of these new provisions awaits only the completion of study by Congress of measures suggested by lawyers and accountants.

The measures are in some cases extremely complicated, dealing with highly technical provisions of the law relating to corporations, partnerships, estates and trusts. Congress generally leaves it to the committees concerned to make such technical changes in the law. Relying on the drafting skill of the specialists, the measures will go through without serious argument once they are completed.

"Tax people"

Among the loopholes the measures are designed to close is one that permits movie companies, for example, to sell rather than distribute their completed film story, then collapse the firm and distribute the profits to the participants to be taxed at 25 per cent capital gains rates rather than at the higher income tax rates.

Another provision would discourage the purchase of unprofitable companies by those that are profitable in order to apply the losses acquired as a credit against taxes. The Congress will also legislate to keep individuals from dividing their personal incomes into several "tax people" (their close relatives) via multiple trusts so as to pay several tax bills at low-bracket rates rather than one bill at a steeply progressive rate.

These, then, are changes in the tax laws that are likely to be made in the coming session of Congress. They may not be as comprehensive as impartial students of the subject would wish to see, but they do have the important virtue of being feasible—and politics, after all, is the art of the possible. ■

THE YEAR THAT GLAMOUR FADED

by SAM SHULSKY

■ WITH THE FIRST YEAR of the "Soaring Sixties" having come to an end, even the most sanguine stock market habitué would be glad to settle for a change in name to the "Sobering Sixties."

In fact, so far as Wall Street is concerned, all the "soaring" last year was confined to one day—ironically enough, the very first. During that initial stock market session of the Sixties—January 4, 1960—the old faithful of stock market averages, the Dow Jones 30 Industrials Index, reached a new all-time peak of 688.21. That was its "finest hour." Thereafter, the over-all trend was down—and often precipitously so. The 10-year-old bull market that had gotten under way in mid-1949 seemed to have collapsed.

What happened? For one thing, business did not soar after the settlement of the longest steel strike on record; instead, it deteriorated. While consumer spending indices held at record levels, heavy industrial production and profits declined. Although the public continued to spend large amounts of money on soft goods and services, "large ticket" sales declined steadily, and industry itself curbed its capital expenditures programs for the future.

The more pessimistic argued that the classic, postwar depression, initially halted by the outbreak of the Korean war, was now upon us. Others shrugged off the setback as merely another recession not unlike those in 1948 and 1953. Neither group, however, foresaw anything so serious as the 1929-32 depression.

The trend of business alone does not account for all that happened in the 1960 stock market. For Wall Street refuses to be guided by statistics alone, any more than a glamorous woman will dress for a winter ball strictly according to the thermometer. The stock market, too, is influenced by considerations of "glamour."

Glamour in the stock market might be described as that quality which leads the buyer to believe that a stock will never cease to grow better and better. It is evaluated from day to day by the changing emotions of millions of men watching tickers anywhere from Hong Kong to Zurich. In the decade of the "Fabulous Fifties," the enthusiasm for the glamour factor in stocks was higher than at any time since the 1920s.

Background statistics bearing on the prices established during the long bull market of the 1950s and a brief analysis of them will show how important a role "glamour" played in maintaining market optimism.

"Earnings" on the Dow Jones Industrials Index stocks were at $30.70 in 1950 and the "dividend" at $16.13. These figures are, by most modern standards, quite favorable. Yet stock market traders and investors that year kept the industrial average in a range between 194 and 236; the median was 215. This means that they were willing to pay no more than seven times annual earnings for stocks and would take no less than a seven and one-half per cent yield for putting their money out at risk.

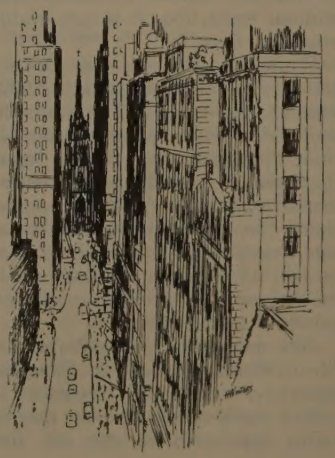
Except for a pause in 1957, the trend of stock prices throughout the decade was steadily higher. By the close of 1959, the industrial share index ranged between 571 and 683, with a median figure of 627. Earnings and dividends, it is true, had improved. But not enough to explain such an increase. Earnings had climbed about 12 per cent through 1959 to $34.31 for the same index and dividends were up about 22 per cent to $20.74.

This means that the stock buyer of 1959 had become so starry-eyed about the future, about the "new plateau" of stock values, about the one-way street for share prices that he was willing to pay 18 times earnings for the conservative stocks in that average (and many, many times more for "hot" stocks). Furthermore, he was willing to put his money into common stocks for a dividend return of only 3.2 per cent—at that time far less than he could have received in government bonds or in government-insured savings accounts.

During the boom, stock market analysts were busily drawing lines which proved to anyone who would take time to follow the line into the future that if a company earned $1.50 in 1955 and $2.00 in 1956, it was only reasonable to expect that the 30 per cent improvement would insure a per share earnings figure of $2.60 in 1957 and $3.38 in 1958. In this atmosphere of optimism, where people believed that earnings would inevitably increase, stock prices mounted.

The tendency to draw lines and project future growth was spurred by the fact that many of the stocks being given this *reductio ad absurdum* treatment were shares of companies involved in fields very few understood but everyone was excited about.

The optimists reasoned that if a person were content to pay 15 times earnings for a company making breakfast porridge, he was bound to be willing—nay, eager—to pay much more for a company making semiconductors, transistors, microwave equipment or cosmic communica-



tions devices. Clearly the limit was in outer space.

No one familiar with Wall Street should be surprised to learn that it all got a little silly. The word "electronics" or even "tronics" became the password to stock market success. Owners of small companies making bed table lamps or toasters were able to "bail out" of their stock at high prices by merely inserting the magic word in their firm's title. They found that there were fortunes to be made by letting the public in on old family enterprises. And new companies were being set up almost daily by promoters who hinted at mysterious 21st-century research projects within the walls of what proved to be rented Long Island garages.

And if the company was a going organization, with a demonstrated ability to produce that new magic item of the century—transistors—the public's eagerness knew no bounds. A privately owned company that made transistors and that had been formed only a few years previously saw an initial offering of only one-seventh of its stock snapped up by the public at roughly 350 times the company's total original capital.

Boom, boom, boom

This frenzy was not confined to electronics. At one period or another, the public discovered the boating boom, the camera boom, the mutual fund management stock boom, the credit card boom and the savings and loan management company boom. In each case they bid recklessly for these stocks confident that no matter what price they paid, a bigger fool (or bigger enthusiast) would come along tomorrow willing and able to pay a higher price.

The peak of this excitement came in mid-1959. Taking full advantage of 20/20 hindsight, we can now determine that the start of the long steel strike marked the beginning of the end of climbing business and rampaging markets, even though stock prices continued climbing to the very end of the year.

The steel strike ended on the last day of the 1950s, and the stock market community turned to the new decade with a high heart. Thus, it was a cruel blow when it became apparent that there was no rush to buy steel once production was resumed. A strike nearly six months long had not brought any significant shortages in steel, nor in appliances, nor in construction nor even in automobiles. All through 1960 the steel production index continued drifting lower. And toward the end of the year the word "recession" was being spoken aloud even in polite company.

Although this was bad enough for the steel and other heavy industry shares, it could not help taking the fine edge off the appetite for the glamour stocks as well. It's all very well to become excited about new boats and outboard motors and transistor radios and savings and loan and mutual fund managements. But if the nation's basic industries are ailing, and unemployment rises steadily, where will the Good Time Charlies, the mutual fund buyers and the outboard putt-putters come from?

At the same time, the domestic economy was hit by severe competition from abroad. Not only did the sales of domestic goods decline, but profit margins dropped. As a result, the year saw a monotonous series of "higher sales, lower net profit" corporate reports. Dividends followed the same discouraging trend. And Wall Street began to write down the price it would pay for future growth prospects.

Sobering influences were emanating from many areas totally unrelated to the world of finance. Not the least of these was the international unrest following the collapse of the summit conference in Paris. Suddenly the cold war was upon us in all its old fury. It seemed as though a goodly portion of our people simultaneously awoke from what had been a long dream.

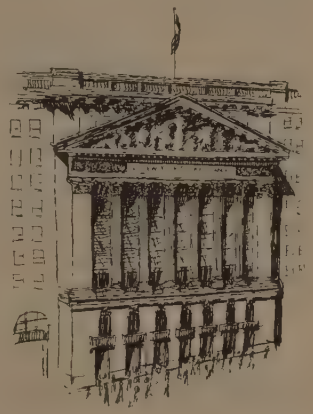
From "power" to "economy"

The automobile industry, to take an outstanding example, suddenly began talking economy. Horsepower —which had risen past the 300 mark —was drastically cut back to 100 and even below. Car lengths and weights were trimmed. Supplanting all the previous talk of "fast getaways" and "surging power" we now were getting lectures on high gas mileage and economy of maintenance.

Other fields were similarly affected by this seeming return of sobriety and economy. Men's clothing makers reported some return to staid suits from the previous sports jacket spree. The paperback book business soared. And the nation's best-seller book lists sported at least two volumes which chided us for our wasteful habits.

All this helped to drop the price of Polaroid from an extreme high of 261 to an extreme low of 163; of NAFI—the boat builder—from 67 to 13; of Texas Instruments from 256 to 148; of ABC Vending from 42 to 23; of Automatic Canteen from 52 to 21.

The ebullient mood which had greeted the start of the Sixties was evaporating. In such an atmosphere, people putting their money out at risk were a good deal more cagey than they would have been a year earlier. And they may be expected



to continue being cagey for some months to come.

One of the most interesting gauges of the enthusiasm which makes for high stock market prices is published by Arthur Wiesenberger & Co., the Wall Street brokerage firm and mutual fund authority. It is called, and aptly enough, the "senti-meter."

This graph charts the stock market record since the beginning of the century. Superimposed on it is a line showing the market price the public has paid during the last 60 years for $1 of dividends. The reasoning behind the chart is obvious. When investors are optimistic, they are willing to pay a high price for $1 of dividends. When they turn cautious, they drop their bids.

During this century, periods of optimism have led investors to bid an average high of $33 for $1 of dividends. Or, in other words, to put their money out at risk for a three per cent return. In May, 1936, just before the New Deal's recovery program suffered its first big setback, a high for this century was set at $36.90. Stock market money was going for 2.7 per cent!

At the other end of the scale were the periods of fear and outright panic which caused investors to drop their bid to an average of $12.50 for $1 in dividends, an average yield of eight per cent. The Great Depression brought the price down from a boom level of $33.62 to $10.02, and recent years have seen a "bottom" established around the $15 mark.

Despite the substantial reduction in stock prices over the last year, this index is still relatively high. Although it has come down from the $34.24 level of July, 1959, it is still around the $30 mark—historically a high price which has almost invariably in the past been followed by at least a short-term decline in general stock market price levels.

Although very few in Wall Street see a collapse approaching similar to the Great Depression, there are more than a handful who foresee retreats in both business and securities prices on the scale of the 1953 and 1957 recessions.

Ralph A. Rotnem of Harris, Upham & Co., an outstanding student of stock market history, wrote recently: "Now that some of the glamour has gone out of the more speculative issues, there is a revived interest in the study of values and the relationship of the stock market levels to such significant influences as earnings and dividends. It is interesting how investors come back to such a solid anchor after speculative sprees die out."

He then proceeded to tabulate how the cost of buying $100 worth of earning power in industrial securities has risen steadily in recent years. Back in 1949, his figures show, you could have purchased this amount of earning power for $1,030. In other words, a 10-times earning ratio obtained. By 1953 it had risen to $1,160; by 1957 to $1,440, and recently to $1,800. In the last 25 years, Mr. Rotnem calculated, the average cost was $1,520. To get back to that ratio, the Dow Jones averages (then around the 600 area) would have to recede to about the 480 mark.

Neither of these experts, nor any of the group who influence Wall Street thinking, would want to imply that Wall Street and the field of investing in general can be run on a strict slide-rule basis. Nor should it be. But these statistics and reasonings are part of the overall climate which does affect the stock market.

In general, the stock market analysts, the economists and the lay public are still faced with the problem of properly labeling the state of business in the U.S. and, indeed, in the world.

Is the current letdown—as many believe—merely another recession which will blow over as did the 1953 and 1957 setbacks? Or is it only the first stage of the traditional postwar depression which has heretofore, without fail, accompanied the completion of recovery from war, the filling of long-empty pipelines, the satisfying of long-felt wants? In addition, what will be the effects of the continuing cold war crisis? These are questions no one can answer with certainty. And it is uncertainty the stock market cannot abide.

All in all, it seems that the Fabulous Fifties are past and the Soaring Sixties have not yet begun. The glamour stocks' "winning streak" has been broken and it will not be easily resumed. Even a "hot" base stealer must come back to touch base once in a while. ■

The gold crisis reviewed

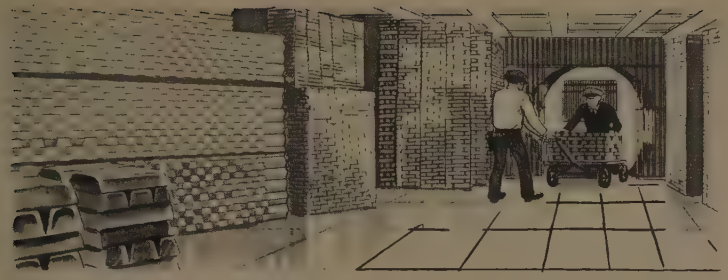
A Bullion-Dollar Problem

by JOHN McKNIGHT

■ SOME 15,000 dependents of military personnel will be returning each month to the United States through July, 1962, in an attempt to reduce Defense Department overseas spending by up to $1 billion a year. This is part of an attack on our gold losses which were $1.9 billion last year, following outflows of $1.1 billion in 1959 and $2.2 billion in 1958.

The losses reflect our current unfavorable balance of payments. The U.S. balance of payments is the difference between what the U.S. and its residents owe abroad and what is owed to us. Settlement of this difference can be made in two ways—either by a transfer of ownership of gold, or by an increase or decrease of credits to foreigners in United States banks or to U.S. residents and corporations in foreign banks.

Credits can and do accumulate on both sides of the Atlantic. However, the build-up of foreign credits in the United States in the past five years has been far in excess of the build-up of United States credits abroad. Short-term assets of foreigners in United States banks were $21.2 billion on September 30, 1960, about $7.5 billion higher than they were five years before. These assets amounted to 63 per cent of our gold stock at the end of 1955; they now exceed it by more than $3 billion. If all such assets were to be claimed at one time—a most unlikely occurrence



--the $17.6 billion in the U.S. gold stock as of the end of 1960 would be wiped out.

The gold that is "lost" does not actually leave this country. The Federal Reserve Bank of New York stores at no charge the gold of 72 foreign governments, central banks and international agencies. When a foreign central bank or government converts assets to gold, the gold is sent from the Assay Office of the Treasury to a vault in the New York bank some 80 feet below ground. There it is placed in a cage marked for that foreign bank or government. The Federal Reserve bank also rearranges the gold, which is in bars worth about $14,000 each, to make payments from one foreign government to another.

What are the factors that lead to a gold loss? This can best be shown by listing the items making up the total payments between the United States and foreign countries.

The United States must pay abroad for:

- Imports of goods and services.
- Remittances and pensions sent out of the country.
- Government assistance and related payments.
- Private and other government capital outflows.

The United States receives payments for:

- Exports of goods and services.
- Repayments on United States government loans.
- Foreign long-term investments in the United States.

The difference between payments and receipts is met by changes in the gold stock and in short-term balances of foreigners in United States banks.

Exports of goods and services include merchandise, military supplies and services transferred under government grants, transportation and related services furnished by U.S. companies, travel of foreigners in the United States, military transactions and income on foreign investment.

Imports of goods and services cover roughly the same groupings. However, military supplies and services do not appear, since there is no such transfer from foreign countries to the United States. But the item "military expenditures" does appear in the import total; it represents goods and services purchased abroad by the Defense Department. This now makes up a substantial outlay each year, quite apart from economic and military assistance. It totaled $3.1 billion in 1959 compared to less than $50 million a year before World War II.

Record trade levels

The largest items in our balance of payments are merchandise exports and imports. United States exports and imports have reached record levels in the past four years, as has total world trade. But our exports reached their peak in 1957 and have since declined, while our imports continued to rise. Exports topped imports by $6.1 billion in 1957 but by only $910 million in 1959.

There was some recovery last year to an export surplus of more than $4 billion. But can we expect that exports will continue ahead of imports? Not necessarily. Changes have occurred in the competitive position of Western European nations and Japan. These countries are now more self-sufficient and can produce many products which compete with or undersell those of the United States.

The economies of many foreign lands have grown stronger, and U.S. industry and government have contributed to that strength. The contributions of the government appear in the balance of payments as unilateral transfers. The contributions of industry take the form of private capital flows. These governmental transfers and private investments involve the flow of funds out of the country. They therefore appear as debit items in the balance of payments.

Transfers or grants of the United States government are expected to return dividends in the form of increased security to the free world. Investment abroad by U.S. manufacturers is aimed at increasing their profits. American manufacturers want to participate in Europe's growth by having manufacturing facilities overseas. This will make it possible for them to sell competitively in markets abroad and, in some instances, will enable them to ship products to the United States at a lower cost than goods manufactured at home.

Security and profits

From one standpoint this is all to the good. Government grants of $3.5 billion to $4.5 billion yearly are expected to yield increased security. Increased foreign investment by United States industry is intended to help profits.

But from another standpoint, the export of private capital tells us something about our own economy. For some products there is now a wide gap between the cost of manufacturing here and abroad. The Worthington Corp. found, for example, that manufacturing costs of three of its pumps and compressors, in the most economical of its European plants, were less than 50 per cent of those in this country. Moreover, its costs here have risen from 35 to 45 per cent in the last five years, as against small decreases in its best European plant.

These differences are contributing to the movement of capital from this country. For companies set up or purchase manufacturing facilities overseas to take advantage of lower costs.

In the past, high wages have not hindered the United States from finding export markets for its manufactured products. Neither have they meant any great influx, except in the past five years, of foreign manufac-

tures. High wages here have generally been justified by high productivity.

But the rebuilding of European and Japanese industry after World War II has meant a large investment in new facilities. As a result there have been substantial increases in output per man-hour. There have been increases in wage costs, too, but these are still well below those of the United States.

Manufacturing abroad is therefore more competitive with U.S. manufacturing than it was five or 10 years ago. This is shown by the fact that imports of finished manufactured goods in 1960 were more than 50 per cent higher than in 1957, while exports of such goods were a little lower.

A few economists are of the opinion that the United States is now in a "fundamental disequilibrium." By this they mean that costs and prices here have risen out of line with costs and prices abroad. If this is so it is a development that can only mean a further worsening of our payments position.

The correction of such a disequilibrium would involve a readjustment of cost and price levels through a process of deflation in the United States. In the past such a remedy was possible. But it is unacceptable in today's world. Now, no political party could stay in power if it chose the route of deflation to correct such an imbalance.

A fundamental disequilibrium could also be tackled through devaluation of the dollar, reducing the value of a dollar in terms of gold. Devaluation would mean that United States goods would no longer be high-cost goods in terms of other currencies. A machine priced at $500 before devaluation and costing a certain number of German marks could be bought after devaluation for a lesser number of marks.

But the chances of a successful devaluation are small. Following a U.S. devaluation, other leading countries could also devalue their currencies proportionately. This would be a protective measure to prevent the U.S. from gaining a competitive advantage in world trade. As a result, the situation after devaluation would be much the same as before. It is, of course, possible that other leading countries might agree to let the U.S. devalue by itself, in the interest of a restoration of stability in our payments position. But it is by no means certain that such an agreement could be reached.

A general devaluation would, as well, mean a rise in the dollar value of gold stocks of all foreign countries, including the Soviet Union. Russia is a leading gold producer but keeps secret the amount of such production and the size of its gold stock.

We must look elsewhere for solutions to the problem of the gold losses of the United States. Can these be found in policies that affect other categories of goods and services—transportation, travel, military expenditures and income on investment?

Exporters and importers in this country pay shipping and insurance companies here and abroad for transportation and insurance. Foreign exporters and importers likewise hire the services of United States and foreign shipping and insurance companies. In 1957 there was a net credit of $400 million in favor of the United States from transportation. By 1959 the balance was $125 million in favor of foreign transportation. This amounted to a net loss of $525 million over a two-year period.

Preliminary data show that the balances in favor of foreign transportation widened further in 1960. The Commerce Department is attempting to combat this source of deterioration by urging business to make greater use of U.S. air and sea transport.

Last-ditch measure

Differences in the travel account are more significant. Foreign travel by United States citizens was valued at $1.6 billion in 1959, more than $700 million higher than travel by foreigners in the United States. Before and immediately after World War II, this net difference averaged about $200 million a year, but since that time it has grown steadily.

The United States could, if necessary, restrict foreign travel or limit the amount of money each person can take out of the country. Other nations have done so. But this would be a last-ditch measure.

More can be done with military spending overseas, which currently is $3 billion a year. This spending is not offset by foreign military spending in this country, which hardly exists.

Some part of this money goes to support the 484,000 dependents of armed forces personnel who live overseas. Another part pays for supplies purchased abroad for troops and dependents. Under President Eisenhower's recent directive, the return of 284,000 dependents this year and next may mean a cut of up to $1 billion in these outlays.

Income from foreign investments constitutes a bright spot in the services sector of the balance of payments. Return on direct investment abroad, that is, earnings of foreign affiliates of U.S. companies, was $2.2 billion in 1959. Income from other private investment added another $500 million; and income from in-

vestment by the United States government was $200 million. This total of $2.9 billion was offset by $1 billion earned by foreigners on their investments in the United States.

The balance of $1.9 billion in favor of this country represents a solid and growing item in our international receipts. It has risen from a prewar net of between $300 million and $400 million a year, and is likely to continue rising in view of the jump in private investment abroad in the last four years.

This brings us to the capital account in the balance of payments. The items discussed up to this point are included in the current account. Capital movements are part of the capital account, but income from them is included in the current account.

United States firms have exported large amounts of capital in recent years to take advantage of foreign markets and lower labor costs abroad. The outflow averaged $2.8 billion a year from 1956 to 1959, dropping to $2.3 billion in the latter year but rising again in 1960.

This export of capital is, at present, a drain on the balance of payments, but will have long-run benefits. As noted above, income from private investment abroad is rising; now, it even exceeds the total of new private capital sent abroad in 1959. In other words, total investments abroad are already so large that the yearly return is sometimes in excess of the sums being exported for new investment.

Government capital outflows include U.S. government loans through such institutions as the Export-Import Bank, and loans made under our economic aid and security programs. These latter are to be distinguished from direct military and economic assistance by grants.

Net drain

Long-term loans by the United States government have been generally running around $1 billion a year in recent years. They rose, however, to $2.4 billion in 1959 as a result of a payment of $1.4 billion to the International Monetary Fund. But yearly repayments on these loans have been running at upward of 50 per cent of the amount flowing out. While there is thus a net drain on the balance of payments from this lending, it is an account in which repayments are being made.

The capital account is offset partially by an inflow of foreign capital. This must be separated into a long-term and a short-term component. The long-term component represents investments by foreigners in U.S. companies and securities. The short-term component represents a build-up of foreign short-term balances in United States banks.

The latter have resulted for the most part from deficits in our balance of payments over a period of years. As such, they represent a further threat to the gold stock of the United States. It is a threat which can be made effective at any time should there be a loss of confidence in the dollar. The reduction of these balances by their foreign owners can be done only through transfers of gold. In this sense, gold is the final means of settlement.

Hence, the build-up of foreign capital in the United States represented by short-term liabilities is, from one point of view, a stabilizing factor in our balance of payments, since it represents a temporary credit item. But the increase in short-term liabilities is also a possible source of imbalance at some date in the future. The accumulation of short-term capital owed to foreigners resembles, to some degree, the British situation in 1931.

At that time, Great Britain's banks had a large volume of short-term liabilities. As confidence in the pound waned in the early months of 1931, foreigners began to reduce their balances in British banks by taking payment for them in gold. England did not have nearly enough gold to continue to meet this kind of drain and was, in consequence, forced to suspend payments in that metal.

After World War II there was a highly publicized "dollar shortage"; foreign countries were unable to get enough dollars to buy the goods and services to promote recovery. In contrast, we now have what may be termed a "dollar glut." The evidence for this is the $21 billion of short-term liabilities now owed to foreigners by United States banks. These balances totaled only $13.6 billion in 1955 and $8.6 billion in 1950.

"Unilateral transfers" are another major item in the balance of payments. These are transfers for which no return in goods or services is expected. An indemnity paid by a defeated nation after a war is a classic example. Remittances sent by immigrants to relatives in their country of birth are another. The latter, by the way, create a net deficit for the U.S. of about $550 million a year.

The unilateral transfers of most importance, however, are grants of military supplies and services under the mutual security program, and other grants under our economic aid programs. Lend-Lease accounted for the major portion of grants in World War II. After the war, aid through UNRAA, Greek-Turkish aid, Chinese military and naval aid, and the distribution of civilian supplies to Europe were the major grants.

Net difference

At present, unilateral transfers by the United States government are running at about $3.6 billion a year. If we exclude military transfers and pensions, the total is about $1.5 billion. It can be argued that the military transfers are for the protection of the United States and are a necessary expenditure. A reduction in grants would therefore have to come from those that are used to build up the economies of various countries throughout the world. It would seem that some relief to the United States balance of payments may be found in this category of expenditures.

To sum up, the net difference be-

GOLDLESS PARADISE?

By mid-1961, according to a recent spoof in *The Economist* of London, the Federal Reserve will "cease" buying and selling gold, with the International Monetary Fund assuming these functions for six months only. The result: everybody, including Mr. K., will rush to unload their gold hoard with the IMF. The resulting wealth will make everybody happy and lead to a universal expansion of living standards without foreign economic aid. The only fly in the ointment: How do countries settle their debts in this Brave New World?

tween all payments made to the United States or its residents and all payments which the United States and its residents owe abroad are made up in two ways: either by a movement of gold or by a change in the total of short-term balances owed to foreigners. The persistent unfavorable payments balance of the United States in recent years has been masked by a substantial rise in short-term balances owed to foreigners by United States banks. It has been more evident in the decline of our gold stock by $5 billion since December, 1957. Taken together, these changes indicate that the United States will have to take some kind of action.

Such action can include (1) measures which will further stimulate U.S. exports; (2) a gradual reduction in foreign aid and military assistance; and (3) measures to stimulate the productivity of U.S. industry. The latter action would have two effects. It would increase the competitive power of American products both within and outside this country; it would also probably lead U.S. firms to lessen their capital exports and to allocate a larger portion of their investment budget to plants within the United States.

Much has been learned about balance of payments problems since the massive disorganization of exchanges after World War I and during the Great Depression of the 1930s. Now, most nations will not hesitate to use several weapons which can protect them against balance of payments difficulties during periods of stress. These weapons include exchange controls, import quotas, restrictions on travel, barter agreements, limitations on capital movements and even devaluation.

Chief source of liquidity

The function of all such measures is to protect a country's vital reserve of international means of payment. These means of payment can include currencies which are sound at a particular time, such as dollars in the postwar period, German marks at present or British pounds at various periods. But the chief source of international liquidity continues to be gold.

This metal has for centuries been the arbiter in the settlement of accounts between nations. While its use is presently being economized through the build-up of foreign balances in one country or another, it is—and will probably continue to be—the final means of settlement.

A continued excess in a country's liabilities abroad over payments due to it must eventually result either in the artificial restrictions noted above, in devaluation or in a decrease in the size of its store of gold. Restrictions on trade or capital movements have no place in a freely functioning world economy. Devaluation is acceptable only under exceptional circumstances. Continued depletion of a country's gold stock is therefore a signal of a dangerous degree of imbalance in its international accounts. It is a stern warning that corrective steps are necessary. ■

Automation and displaced workers

THE HUMAN EQUATION

by EDWARD T. TOWNSEND

■ PROBLEMS ARISING FROM the impact of technological change, including automation, are pressing today. We are not entering the age of automation; we are in it. According to a survey by the Institute of Industrial Relations at Berkeley, Calif., in 1955 some 16 per cent of American industry was "extensively automated," and 39 per cent is expected to be by 1964.

We cannot look to the past as a guide to what effect technological changes will have on employment. Most of the automatic devices installed so far were put into operation during periods of high level employment and business expansion. Moreover, it is hard to pinpoint unemployment caused by technological changes; reductions in employment due to automation and other developments are difficult—perhaps impossible—to separate from other factors causing layoffs, such as general economic conditions, costs and competition.

Often, according to an economist of the Labor Department's Bureau of Employment Security, automation may cause companies not to hire new workers rather than lay off old workers. The problem is one of shrinking employment opportunities.

Moreover, the impact of automation may be diffused. Automation in a Detroit auto plant created technological unemployment in South Bend, Ind. suppliers' shops; dieselization of railroads is partly responsible for persistent unemployment in railroad shops in Altoona and Philadelphia, Pa., and automation of textile mills was a major factor in the industry's shift from obsolete Northern textile centers to new mills in the South.

In the rubber industry, according to the United Rubber Workers, tire and tube manufacturers are now getting about the same output with 30 per cent fewer workers and 29 per cent fewer hours of work than they needed a decade ago. The union estimates that at least 31,000 jobs have been lost to "new technology, new machines and new equipment" in tire and tube plants alone.

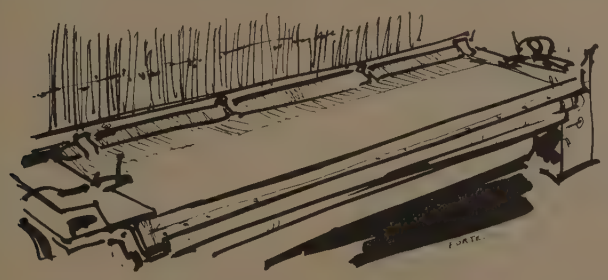
Railroad employment in October, 1960, dropped to the lowest level since 1900—885,000 as compared with 909,000 in October, 1959, and a peak 2,022,832 in 1920. The Railroad Retirement Board, which handles rail unemployment insurance, blames increased mechanization and "a lot of other things" for the decline in jobs. Railroad brotherhoods and nonoperating unions contend that technological changes are *the* big factor.

The auto industry's steadily in-

creasing use of automated equipment has cut into employment, not only in the plants but also in the offices. In 1959 the average employment in production in the auto industry was 573,600; production stood at 6,700,000 vehicles. In 1956 there were 75,000 more plant workers producing only 200,000 more vehicles. That means that about 75,000 workers, nearly all of them poorly educated, unskilled hands, have been weeded out of the factories; the chances are they will never be needed there again.

Local 889 of the United Automobile Workers, a white-collar local that represents office workers in Chrysler plants in Detroit, lost 1,000 members (declining from 5,000 to a recent 4,000) almost entirely because of "inroads of automation in offices," according to the local's president, Wallace Webber. One change cut the number of payroll clerks needed from 200 to about 60. The machines installed in that department "don't get tired or have to be paid overtime rates," Webber said, so Chrysler is expected to use them on other accounting work, further reducing the need for clerical help.

The Oil, Chemical & Atomic Workers claims automation has elim-



inated "tens of thousands of jobs" in the industries it covers. The United Steelworkers places job losses in its field much higher. All in all, the AFL-CIO says that some 800,000 industrial union jobs have been "automated away" in the past five years.

Most employers are unwilling to talk about the impact of automation on the number in their work forces. They may admit "temporary" displacements, but few will concede substantial reductions. Some deny them. The Ford Motor Co., for one, said some time ago that it absorbed skilled workers displaced by automation in engine production operations and that the total it employed in the skilled classification rose by 976. The UAW countered by noting the figures used by Ford were for a skilled classification only.

In some cases, however, automation may lead to an *increase* in employment. The Division of Productivity and Technological Developments, Bureau of Labor Statistics, U.S. Department of Labor, cites the following examples:

• An insurance company installed electronic computers in a section which employed 800 people, 198 of whom worked in areas directly affected by the introduction of the new equipment. The installation required two years. During this time the 198 were screened to find nine to be trained to operate the new machines. The others were reassigned and, if necessary, retrained; no one was laid off, and no employee had to take a salary cut. Many got better jobs—and more money. Twenty new employees were added, specialists in the electronics computer office.

• An airline installed automatic reservations equipment because the old manually processed system could not keep up with the rising volume of traffic. The carrier announced in advance that no one would be laid off. All employees were trained to work with the new equipment. Within four years employment in the reservations section increased from 259 to 529. More important, all jobs in the section were upgraded. Low-grade monotonous tasks were eliminated, and the number of higher paying jobs was increased.

• A bakery using pre-World War II equipment found that in order to survive, it would have to cut unit production costs by changing over to the latest automated equipment, to be housed in a new plant. The change-over would take two years. The company called in union representatives to begin ironing out, far in advance, matters affecting workers. In a screening process, many workers were found to have talents that could be used in highly technical jobs in the new plant. Some workers were laid off when the move was made; employment dropped 4.4 per cent the first year. But three years later employment in the bakery was six per cent higher than before automation, and the average wage for upgraded jobs in the new bakery was 60 cents an hour higher than before.

Other examples of successful retraining of workers displaced by automation can be taken from the experience of the General Electric Co., a leader in this field.

Some time ago GE decided to shut down a porcelain operation in Schenectady, N.Y. The workers involved had always dealt with porcelain; sons had followed fathers into the plant. The company undertook to retrain all those willing to learn a new skill. Workers were tested for interests and aptitudes; job opportunities were surveyed. The displaced workers were then given training, outside the plant and at GE's expense, for specific jobs. If the training did not develop the skill needed to get a new job, the testing and retraining was repeated. In a few instances men set in past ways failed to respond favorably to retraining until after a third and final effort to fit them into new fields of work at GE or in other plants in the area.

When the GE porcelain plant closed, only a handful of workers were left jobless. Many of the others stepped into higher paying jobs; only a few were employed at lower wages than formerly. The program was a model of what can be done with the help of careful planning if a management is prepared to spend time, effort and money—and if jobs are available for those who can be retrained.

A similar situation arose late in 1953 when GE's plastics department announced that it would leave Pittsfield, Mass., a move that would cost 102 moldmakers their jobs there. By careful planning and much hard

work every one of the 102 was placed. Some, however, accepted lower rated jobs. A year later when the industrial heating department moved out of Pittsfield, and 150 employees faced the loss of their jobs, GE repeated what it had done for the moldmakers.

At Lynn, Mass., GE has a new employment planning staff of three specialists employed full time to look ahead not only two or three months, but a year or more. They study what will happen in the employment area—including the results of new machinery. Using this information, the company can lessen the impact on its employees when changes come.

Moreover, GE's new job opportunities plan written into contracts negotiated in 1960 extends the rights of those who may be displaced. They can be retrained at company expense for other GE jobs. They can also be retrained on the outside—in technical or professional schools—for new jobs outside GE, in any other field of employment. And GE will pay at least a part of the cost. There is an important *if* in the latter plan. It is available only if the displaced worker gives up job rights at GE—his right of recall from an extended layoff, for one thing.

The first permanently displaced GE employee to claim this help asked for tuition assistance for training as a mortician. He had studied in that field before taking a job with GE, and he said it now appeared to him to be a "more secure" type of employment.

Level of education

One basic problem in retraining relates to the level of education of the employees. Studies by the Bureau of Labor Statistics indicate that when new jobs involve significant changes in the level of skill, they are filled from the outside; existing workers are not retrained. This is almost always true when new jobs require professional or technical training.

In one plant, recently, new jobs being created required a sound working knowledge of the use and preparation of blueprints. None of the employees available for retraining had a proper background and aptitude for this work. Too much retraining would have been necessary.

Maintenance workers in automated plants frequently need skills or combinations of skills beyond the practical reach of machine operators or even craftsmen such a machinists, electricians and plumbers. A knowledge of mathematics, physics, electronics, hydraulics and other sciences may be required. Where they are, former factory operatives cannot be expected to shift, even through retraining, into the new work.

Largely because of the basic training that appears to be necessary for the key jobs in automated plants, there is a growing feeling among workers that good jobs will be "limited, almost like hen's teeth," as one operator put it, for men retrained from nonautomated plants. "The future in 'push-button' plants belongs to the college boys and the slide-rule men," he said. "Believe me, we're going to get only what's left over—and the jobs won't be real jobs at all."

Experts say he is unduly pessimistic. They concede that there will be limits on the advancement of factory operatives retrained for jobs in automated plants, but vigorously deny that operatives cannot rise at all. It is a matter of individuals and, in large part, their educational background. The older man with sound experience in an operator's job may be at a disadvantage. The younger man, with more formal schooling in mathematics and the sciences, has a much better base for retraining.

Not all new jobs will require greater skills, but many new operations must be performed more rapidly than the old ones. They require more concentrated vigilance to complex adjustments. A moment's lapse, perhaps only a minor matter previously, could cause costly disruptions in a fully automated process. A factory worker, retrained for a semiskilled job in an automated plant, complained: "I'd rather have to work hard for eight hours than do nothing physical but have to be tense for the eight hours, the way I do now."

This is a substantial problem. The different jobs in automated plants are likely to appeal more to the logician than to the craftsman; they substitute nerve and alertness for muscle and hand skills. Those planning retraining programs, and selecting the men to be retrained, have to take these differences into consideration.

The willingness of workers to be retrained is vital; forced education is seldom successful. But an incentive is generally present if there is a real hope for a better job or a greater opportunity; or if there is fear of no job at all.

Training only for *possible* jobs is just as vital for the success of a retraining program. At a management meeting in Albany not long ago, an AFL-CIO spokesman made that point bluntly. "What's the good of it if there's no job for a worker who takes new training?" he asked. "If the one big plant in town automates and cuts employment, where can retrained workers go?"

Fortunately, automation is usually a deliberate, limited development. It advances slowly and unevenly through a plant or community. The normal attrition of the work force between the start of planning for mechanization and the beginning of automated manufacturing often can be counted on to ease the impact of stepped-up production with fewer employees.

Considerable changes

Nevertheless, automation by its very nature must cause considerable changes. The impact of technological developments will be greatest in big industry—for instance, in steel mills, and rubber and auto plants. The problems created in such industries will be the hardest to resolve.

Generalizations are easy to make—

perhaps too easy. But it is safe to say that automation will mean, at most, temporary displacements in expanding industries, but very considerable loss of jobs in declining industries. It will not have a serious impact where there is normally a high turnover of labor—as among women workers; attrition will take care of the reduced labor needs.

Its impact will be broader, perhaps, than expected. Recent government figures indicate that technological developments may be hitting more echelons of workers; reports to Washington from state employment offices in November, 1960, mentioned a growing effect on middle management and white-collar workers.

Impact and consequences

And the impact could have further consequences. Technological changes that move workers into services are shifting them—and will shift them by increasing thousands—into lower-wage employment. Moreover, communities and even regions will change.

The changes will not always be for the worse. Lawrence, Mass., lost most of its textile mills. For a time, unemployment was high. But civic efforts to bring in new industry have changed Lawrence from a troubled textile center to a relatively high-wage electronics city. Utica, N.Y., fared similarly. But other textile communities in the Mohawk and Hudson Valleys of New York are still distressed, although mills moved out many years ago.

Undoubtedly, automation will have dramatic effects on cities in older areas. When mechanization is being considered, relocation of the plant is likely to come up for review, too. The Electric Autolite Co. is moving plants from Toledo, Ohio, to Decatur, Ala., and Bay City, Mich., where it expects to get more efficient utilization of new equipment. The Goodyear Tire & Rubber Co. threatened to move a big tire plant from Akron, Ohio, unless workers there would agree that if the company spent $10 million on plant rehabilitation and the most modern tire-building machinery, the Akron workers would meet production standards possible elsewhere. The workers agreed; the plant will stay in Akron.

More of this is likely. Operations will be telescoped as automation spreads; older plants will be closed and old communities will suffer the consequences. Unless new industries can be induced to move in—or unless workers move away—new and disturbing pockets of protracted unemployment will be created.

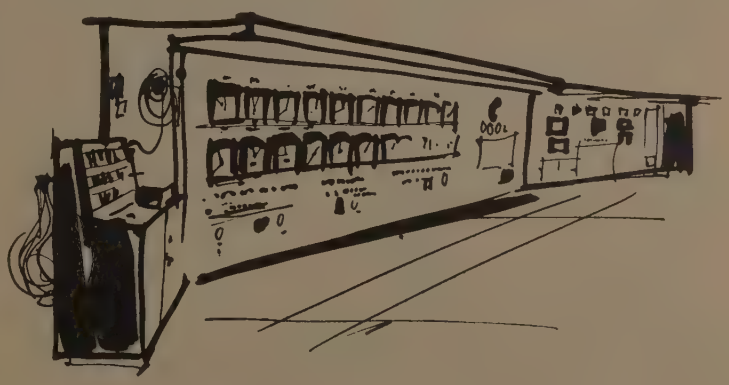
The consequences will be broad and deep. There will be increased expenditures for private philanthropy; savings will be drained away; homes and other possessions will be lost; there will be a general slump in local business; local tax revenues will fall; perhaps there will be a downward spiral into chronic local depression.

It is probable that the new Democratic Administration will tackle this problem of distressed areas—existing and possible future ones—as one of its first legislative projects.

Part of the proposals for action include government assistance in the retraining and relocation of workers in distressed areas and in encouraging an influx of new industries to areas with a surplus of workers, long jobless.

There are basic disagreements on measures in this area—as in others. Particularly, they involve how far the government should go.

One suggestion is that a national Committee on Human Resources should be established, similar to the Committee on Economic Development. The new committee would be charged with promoting the formation of local task forces to assess local needs and endeavor—locally, as far as possible—to meet them.



A Bridgeport, Conn., project is considered a model. Some 311 industrial plants are cooperating with labor organizations and local and state agencies to study present and future personnel needs there and prepare for them. In Waterville, Me., a town survey found shortages of workers in 47 classifications; 600 adults enrolled in new job-training courses at Colby College and in local schools to prepare for these opportunities. The Greater Lawrence (Mass.) Manpower Committee also has done a notable job in surveying and training for needed skills, as part of the shift from textiles to new industries.

Areas of disagreement

The Committee on Human Resources proposals—and others—face heated debate. There is general agreement that something must be done to anticipate the impact of automation—to determine how much of an impact there will be, how fast it will come, where it will hit and what the effects will be on the labor force. There is less agreement about what should be done.

One area of disagreement relates to the seniority of workers. Many unions are concerned about preventing any breakdown in the present seniority system that they won with so much effort. They are inclined to insist that a man's years of service give him a firm and continuing claim on employment—even though retraining for a new and different job is necessary and the nature of the new job may be very different. Further, the unions frequently argue that no new employees should be hired for any jobs as long as workers

are laid off or are subject to layoffs.

During the bargaining in the electrical manufacturing industry some months ago, the president of a large local conceded that union insistence on a strict observance of the seniority system undoubtedly would interfere with management's efforts to fit employees into suitable new jobs. But, he commented: "Management can roll with it better than a man with family obligations and the possibility of no job at all. So it's not efficient! It's better than laying off men on the payroll for 10 or 15 years."

The right to make selections on a basis of seniority and other qualifications is an important point of contention in the growing "management rights" fight in collective bargaining. In a few instances, however, managements and unions have instituted joint programs to study the problems created by automation. The most notable of such cases is the cooperation of Armour & Co. with the United Packinghouse Workers and the Amalgamated Meat Cutters & Butcher Workmen.

"Automation fund"

The meat-packing industry has been hard hit by automation. Old processes have been automated or mechanized. Thousands of workers have lost jobs. Many of them never worked anywhere except in a packinghouse and were not prepared for any other type of work.

In contract negotiations Armour agreed to make contributions, up to a maximum of $500,000, into an "automation fund." This finances the study of problems resulting from plant modernization programs and recommendations for their solution, through retraining, relocation and other devices. The unions concede that "in this undertaking with Armour, we are moving along new and untrod paths," and that there is no certainty that any real help will come out of the study. But, the UPW says, the plan "gives us an opportunity to come to grips with the problem of job losses."

Ralph Helstein, President of the UPW, recently said that once the true situation is known, union and management "have sufficient ingenuity to find solutions." He went on to say, "The major contribution of the 'automation fund' will be the degree to which it helps define the issues, delineate the nature of the problems and suggest the avenues where solutions may be found. If it does this much and one thing more, it will be a success. The additional result that we have a right to hope for and expect is that it will point up the importance of planning on both local and national levels."

A committee established by a contract between Kaiser Steel and the United Steelworkers has been studying the impact of automation on those employed in Kaiser's mills and how technological developments can be put into effect in the future with a minimum of hardship. George W. Taylor, of the University of Pennsylvania's Wharton School, chairman of the steel fact-finding committee in 1959 and of the Kaiser-USW joint committee, stressed recently that the committee is exploring an uncharted field. "Inventive and imaginative" solutions can not be expected quickly, he warned.

The United Rubber Workers and some rubber companies have considered less formal approaches to automation problems. The URW has said that "the widespread dislocation which is caused by modern automatic equipment" necessitates new safeguards for workers—beyond seniority, severance pay, recall rights and so forth. Among the new measures it suggested is retraining to be provided by employers.

Organizations speaking for employers on the national scale, including the National Association of Manufacturers, urge labor-management cooperation on the mutual problems of technological changes. But the NAM insists that "resistance by certain labor groups to labor-saving innovations and their insistence on 'make-work' practices [and] wage increases in excess of productivity" should be included.

Further, the NAM believes that technological unemployment is likely to come, if it does, in "specific occupations and industries, and not on the level of employment generally." Part of it will be offset by normal attrition and the remainder can be handled through rehabilitation and retraining of those affected, the NAM contends.

It believes "it would be foolhardy to adopt any hard set of rules to assimilate automation and at the same time to prevent any excessive unemployment while maintaining economic stability."

Labor, on the other hand, believes that there must be a firm policy—a hard set of rules—under government direction if the heavy impact of automation is to be averted. Eventually, it feels, there must be a shorter workweek.

Commitment to study

The new Democratic Administration of John F. Kennedy is committed to a study of the problems of automation—and to press measures to relieve them. The new Secretary of Labor, Arthur J. Goldberg, former general counsel of the United Steelworkers, has been a strong advocate of labor-management-government conferences on automation and other common problems. He will now press "summitry" officially—with Kennedy's backing.

The NAM and the Chamber of Commerce of the United States are wary about the Goldberg proposal of a tripartite conference—a permanent National Council of Labor-Management Advisers. And the plan has the following difficulty to overcome. Labor and management have linked their willingness to confer to provisos that are unlikely to be accepted.

Labor, in the words of the Steelworkers president, David J. McDonald, would like a forum to develop "some broad method of distributing the emoluments" of automation and other technological developments. Management groups want "featherbedding" and "excessive wage increases" considered, and demand safeguards against any repetition of what they say were the prolabor tripartite actions of the National War Labor Board and Wage Stabilization Board of the 1940s.

Call it summitry or whatever, tripartite activity in the whole area of automation problems is likely to produce more talk—or argument—than progress until and unless labor and management can agree on exactly what will be taken up and what, specifically, will be done about reporting and perhaps acting on conference findings. ■

CHALLENGE NOTES

Sidelights on the passing economic scene

COLD WAR IN THE HOME—Advertising a new "adult game of intrigue," Brentano's says: "You'll enjoy many a lively social evening playing *Diplomacy* with your family and friends. Up to seven players guide independent countries through the anarchy of international politics, making and breaking such agreements as they think best in this hard-hitting adventure in the tactics of negotiation and the strategy of coalition-forming."

► *Had a good time last night; broke up NATO and the Common Market and picked up $12.*

* * *

THYME MARCHES ON—Sales of oregano, a herb similar to thyme, are up 3,700 per cent since 1941. Greatly increased national consumption of pizza, in which oregano is used, is credited

with much of the gain. As an example of economic growth it is unlikely that this figure could be bettered. But a nagging doubt assails us: *Is eating more pizza the best way to win the cold war?*

* * *

ELECTRONIC CONFUSION—According to *Executive's Digest*, engineers operating an electronic translator which turns Russian into English were puzzled when the machine came up consistently with "water goat." An expert examined the original manuscript and reported that the phrase being translated was "hydraulic ram."

* * *

OFFICE STATUS SYMBOLS—For a mere $7.50 you can buy a sterling silver scotch tape dispenser. Your monogram on it is only $1 extra.

► *We're shopping for a wild mink typewriter cover.*

* * *

SHARKS AND SHEEPSKINS—When a fraudulent "college" was exposed in California not long ago, the public reaction was somewhat surprising. After authorities brought charges against the bogus school, it was flooded with applications from people who wanted to get diplomas before it was too late.

► *Apparently the increasing public concern over educational standards is a two-way street.*

* * *

NATIONAL GOALS—In an editorial deploring the increasing role of the federal government in the nation's economy, *The Wall Street Journal* points out that one thing Thomas Jefferson and Alexander Hamilton had in common was a peculiar disinterest in setting forth America's national goals.

► *Obviously, the Declaration of Independence and the Federalist papers make no reference at all to "national goals."*

* * *

GOLD! GOLD! GOLD!—The Union of South Africa's Finance Minister, Dr. T. E. Donges, recently urged a rise in the price of gold. "We do not deny," he said, "that the raising of the gold price would be of great advantage to the Union, but we advocate it mainly on grounds of the contribution this would make to international liquidity, and through this to the development of international trade."

► *A sidelight on Dr. Donges' statement: the annual gold production of South Africa is worth over $700 million; thus, for every one per cent rise in the price of gold, South Africa would receive $7 million a year.*

* * *

MORE ON GOLD—Dr. Reinhard Kamitz, President of the Austrian National Bank, made an interesting comment about the adverse balance of payments and loss of gold in the U.S. in a speech before the National Foreign Trade Convention in New York. "As long as there is confidence in the dollar," he said, "and as long as central bankers all over the world can be sure that they will not suffer any disastrous damages from their dollar investments, one should not look at the gold outflow in the way a rabbit looks at a rattlesnake."

► *Or as an ostrich would.*

* * *

OWNERS IN THE DARK—A survey of stockholders by United Shareholders of America revealed that "51 per cent of those surveyed could not name a single product or service of any company in which they owned stock." Stockholders' answers revealed that some believed that General Motors makes gasoline, Swift & Co. builds trucks and Bell & Howell manufactures aircraft.

* * *

BRAVE NEW WORLD—*The New York Times* reports the invention of a child's "slumber pillow" made to resemble a woman's chest and head. "A face,

wearing a drowsy expression, is framed in long braids. The child places his head on the pillow's chest and an adult wraps the arms around his neck. It is supposed to give a sense of security and keep off the draft."

► *For a real sense of security, why not a "stuffed daddy" on a bedside chair with a book of artificial fairy stories on his lap?*

* * *

WELFARE AND GROWTH—In view of the interest in economic growth, we find the following quotation from Bruce R. Morris' recent book, "Problems of American Economic Growth," very apposite:

"Actually what people are interested in is 'progress' or 'welfare' rather than 'growth'; but the content of these terms is difficult to define because each is a wholly subjective matter. It would be highly desirable if we could develop objective standards that would enable us to develop policies to obtain the greatest possible increase of welfare; but this, in a strict sense, seems to be forever beyond our reach. As a substitute and an approximation of welfare, we concentrate on economic growth, by which we mean an increase in the annual output of goods and services."

► *Which may or may not bring us more "progress" or "welfare."*

Challenge Interview

SOLOMON FABRICANT

Director of Research,
National Bureau of Economic Research

The Science and Art of Economic Growth

Q *Dr. Fabricant, as researcher and teacher you have had an opportunity to study the development of the American economy with some fair precision. We would like you to talk about the prospects for economic growth, a subject which became a big issue during the Presidential campaign. First, would you give us a simple definition of economic growth?*

A Well, most economists would define economic growth as an expansion in the volume of goods and services available to the people of the country.

Q *You talk about goods and services in terms of their availability to people, not in terms of the capacity to produce them.*

A Not capacity, but goods and services actually available. I would include here, of course, as other economists would, additions to the capital equipment of the country. Such additions are also available in the sense in which I am using the word. But capacity alone isn't sufficient. It's what you get out of the capacity that is the real criterion of growth. And an expansion in that volume of output is what we mean by economic growth.

Q *A substantial proportion of our industries is working at something less than full capacity, and has been for some time. Is this a unique experience in the history of the American economy?*

A No, of course not. We in this country, and people in other countries, have always had fluctuations in output and therefore in the percentage of capacity being utilized at any time. This is what we mean by business fluctuations, or business cycles. And even in Russia, I might say, there have been occasions and points in the economy where capacity was not fully utilized.

Q *Would you say that this overcapacity is unavoidable?*

A Some of it is avoidable, some of it is not. Economists want to see an increase in the use of available capacity. But not all excess capacity can be avoided, any more than you can avoid not using your spare bedroom on occasion, or keeping your car in the garage.

Q *What are the mechanics of overcapacity? How did the present industrial economy of the United States get into the situation that it is in now?*

A We're getting off on a question of business cycles. I think economic growth is a process which inevitably involves some fluctuation and change. The very nature of economic progress requires a certain amount of waste in the process of growing. For example, if you improve a process, this means that you are making some other process obsolete. If you invent a new product, you are making some other product obsolete. Obsolescent products, obsolescent processes, are idle capacity and idle products, you see, and are, in a sense, a *sine qua non* of growth and progress.

Q *You implied a moment ago that this sort of thing may occur in other economic systems, as well.*

A Yes. This is obvious even in the case of Russia, as I mentioned. They discovered that they have got an excess amount of aluminum capacity, for example. No one could have anticipated this. No one can tell what technological development will mean in terms of creating new needs and bringing about shifts in what is available and what is not.

Q *Can one say, then, that the so-called distressed areas in certain parts of the U.S. today have resulted from this type of unavoidable and even necessary dislocation?*

A Yes. I won't say that all of it is that. Nor would I want to say that less than full employment in coal mining areas is anything that we want to tolerate. We want to avoid that kind of thing, if we can avoid it at a reasonable cost—either by bringing industry to the distressed areas or by getting the people out of the distressed areas.

Q *Well, in any case, economic growth would help absorb people who have become surplus, so to speak.*

A Yes, of course it would. And I think everybody wants more economic growth, just as everybody wants more of the good things of life.

Q *How do we actually go about measuring economic growth? Do GNP figures provide an adequate measure of economic expansion?*

A Economic growth, as I have said, occurs when there is an expansion in the volume of goods and services

available to the people, including additions to the nation's capital equipment. As far as statistics go, we are interested in *real* gross national product, or deflated GNP. I would add immediately that this does not cover all the good things we want in life. We want not only more goods and services, we also want less of the hard labor that is involved in getting these goods and services. Therefore, I would supplement this particular measure of growth with a measure of the amount of man-hours required to get the goods and services. I would also always keep in mind other important goals, such as freedom of choice, freedom to move around, freedom to work or not to work, and so on.

Q *Dr. Fabricant, it has been said that our GNP statistics do not adequately measure improvements in the quality of goods and services. Do you think this is a correct notion?*

A Yes, I think that is correct. It is the impression of most people that the quality of goods and services produced in an economy like the United States has been improving over the years. Of course, there may be cases of deterioration. We all remember Grandma's bread, for example. But, by and large, there has been an improvement, and our production and price indexes largely ignore this improvement factor. The Price Statistics Review Committee, set up for the Bureau of the Budget by the National Bureau of Economic Research, is exploring this particular question as well as others.

Ways of achieving economic growth

Q *Assuming that everybody wants growth, how do we go about getting it?*

A Fundamentally, we get economic growth in two ways. First, we can get it by expanding the resources that we put into the productive process. This gives us more input and thus more output. Second, we can improve the efficiency with which we use these resources so that we get more growth by increasing the ratio of output to input—that is, of productivity.

Q *Which factor has been more important in the growth of the American economy?*

A I think all of the records of the United States indicate pretty conclusively that we have gotten our growth from both sources. However, I would say that the studies we and other people have made indicate that productivity is far more important than most people realize. I think more attention needs to be paid to the sources of increase in productivity.

Q *Well, how do you go about increasing productivity?*

A People frequently equate technological development with productivity increase. In fact, however, productivity increase results not only from technological development, but from all the other sources of increase in national product apart from those measured by the input of labor and tangible capital. It reflects not only technological development, but also the input of *intangible* capital, which is not measured by the ordinary measures of input. In addition, it also reflects changes in the capacity of workers and of management, and improvements in the mobility of resources, which are important factors in productivity. Incidentally, I would include housing among the tangible capital items that are vital in economic growth—as well as many consumer durable goods which in an economy like ours are part of the capital equipment of the country. It would be foolish to think of the automobile as merely a Sunday gimmick. It is a vital part of our equipment and the prime contributor to the decline of the suburban railroad.

Q *How does intangible capital differ from these items?*

A Intangible capital is that capital which, while vital to production, does not take the tangible form of buildings, equipment, roads and the like. Education, for example, is a very vital item of intangible capital, not only to society in general but also to the individual. Young men with a few thousand dollars make a decision whether to invest this money in a little business or in a profesional career.

Q *Wouldn't you measure the value of such investments, as education, in terms of the amount of money invested in them?*

A Well, one measure of any kind of capital investment is the amount of money invested in it. But I would go beyond that. I think it would be wrong to ignore another kind of investment that goes along with acquiring an education, one which is not usually measured in terms of money but in terms of the time and energy that young people must put into education. How much income does an individual forego while getting a degree? If people in school were in business instead, their time and energy would be measured by a market price. We ought to impute a market price to the educational process also, although that would be difficult to do.

Output per man-hour as measure of productivity

Q *Most people regard output per man-hour as the one vital measurement of productivity. Is it?*

A Output per man-hour is the one measure of productivity that we have been able to obtain statistically for some time. But, in fact, it is not a fully adequate measure. Productivity statistics should take account not only of the input of labor in the form of man-hours; they should also take account of the input of other resources, such as the tangible capital equipment. Therefore, I would measure productivity by output per unit of total resource input, that is, by output per unit of labor *and* capital combined in some appropriate way.

Q *Is it easier to measure the output of labor than of other components of productivity?*

A No, I don't think that is true. Output per man-hour is easier to get than output per man-hour *plus* capital, simply because you don't have to measure capital input. And it is only in recent years that we have been able to measure capital input at all adequately. But this does not mean that output per man-hour measures the output *of* labor.

SOLOMON FABRICANT

Q *What about productivity and labor's rewards?*

A The rewards of any group of factors like labor or capital depend not only on productivity but also on the relative scarcity of these factors in relation to other factors. Thus, the real wage of labor has increased in the United States over the years in an important way because of the increase in national productivity, but also because there has been an increase in the amount of capital per worker. Labor in that sense has become relatively scarcer, and this has affected the wage rates of labor.

Q *In other words, per unit return to capital has decreased in relation to per unit return to labor?*

A Yes, that is right. But I want to stress that the per unit return to capital has decreased only *relatively*. It has not decreased absolutely, and the reason it has not is that capital returns also have profited from the increased national productivity.

Measuring quality improvement

Q *Dr. Fabricant, do you think it is inevitable that the rate of productivity of an economy such as ours, in which most of the population is engaged in activities not directly related to the production of physical commodities, will eventually decline?*

A No, I would not say that this is inevitable. I think we are partly captives of our methods of measurement, which do not adequately measure the output of services. Our measurements do not take adequate account of quality improvement, and the services certainly have shown vast quality improvements. We would all agree that the value of a particular volume of medical service, for example, is far greater today than it was some years ago in terms of what it can do to keep you alive and put you back on your feet. You and I know very well what used to be the death rate from pneumonia. We know that tuberculosis sanatoria are now being converted into winter resorts, and so on.

Q *So you do not anticipate any difficulty in maintaining productivity improvements as we shift more and more to services?*

A One does not follow the other. I think if you look back at the history of the United States you won't find any evidence to support the notion that an increase in the relative importance of the service industries leads to a slowing up of the rate of growth and productivity. The service industries have grown very considerably since World War I. Yet the period since World War I has shown a bigger rate of increase in productivity than the period before World War I. I see no reason, therefore, to believe that in the future the increase in services must necessarily mean a diminution in the rate of increase in productivity.

Q *Could you give us an example of how productivity has been increased in a service area?*

A Well, people may think that dentists operate much the way as they used to 50 years ago. But if they stop to think for a moment, they will realize that this is not true. Fifty years ago the dentist either used a foot treadle to turn his drill, or a slow-speed electric motor. The modern dentist uses a high-speed electric motor to run his drill. In fact, the drill runs so fast that he has got to have a cooling liquid to apply to the tooth at the time he runs the drill. Think of all the other improvements that have been made in dentistry. The x-ray, for example. Improvements in the materials used to make fillings, to make bridges. Improvements in our knowledge of the sources of disease of the gums, and so on. There has been a vast improvement in the speed with which dentists work and in the efficiency with which they work, and in the quality of their work. And I say that this means that productivity in dentistry has increased enormously, and I would not at all be surprised to find that it has increased more than in many manufacturing industries.

Q *And, therefore, you conclude that research and technological developments have been as important in dentistry, or even more so, than in manufacturing?*

A I would certainly say vastly important. Nobody really knows how important, but it would be foolish to assume that it is not important.

Growth of GNP

Q *There has been a great deal of criticism of our so-called slow rate of economic growth. Some have said that it is absolutely necessary to take measures to attain a five per cent growth rate. What has been the historical growth rate of the U.S. economy since the end of the 19th century?*

A In the U.S. as a whole, the gross national product measured in dollars, but deflated to get rid of the price factor, has been growing over the past 70 years at something like three and one-half per cent per annum.

Q *That is a long-term average?*

A A long-term average, that is right. The growth measured thus was somewhat faster up to World War I than since World War I largely because in that earlier period the population of the country was growing much more rapidly than at present. Higher birth rates and a lot of immigration were the responsible factors.

Q *Where does productivity fit in?*

A Now, I mentioned before that growth and output can be broken down into two components. One is the input of labor and tangible capital, and the other is productivity. It is interesting to note that the productivity element has been not only important but has been of growing importance. For example, over this 70-year period, output per unit of total input has grown on the average of about 1.7 per cent per annum. But in the period since World War I this has been more like 2.1 per cent per annum. The period before World War I it was 1.3 per cent per annum. So we have had a degree of acceleration in the rate of increase in effi-

ciency, and this has offset some of the decline that has occurred in the rate of growth of resources, population and the tangible capital combined.

Q *Would you say that this somewhat slower pace of growth since World War I is a satisfactory level?*

A No, neither I nor any other economist would find any improvement satisfactory. We always want more. Not only economists, but noneconomists as well always want more. I think the economist would want to emphasize that while we want more, there is a degree of competition among the various things we want. We not only want more goods and services, we also want more leisure. In some degree there is competition between the two. We have had both, of course, over the years. But you could have more goods, if you took more of our increase in productivity in that form and less of it in the form of more leisure. Also, we want a larger degree of stability, for example, in the economy. But there is some competition between the rate of growth and the degree of stabilization. For example, I am sure that we could have all the stability we wanted. However, I think we would have to pay too much in the form of a diminution in the rate of growth. These are competing objectives, and we have got to get a reasonable, sensible balance between them. And we need more economic knowledge so we can get the best combination.

Differences in rates of growth

Q *Insofar as this art has already been developed, how would you as an economist decide whether we need a three per cent growth rate, a four per cent rate, or what have you?*

A Well, before we get into that, I ought to say this. People have been worried about our relative position in the world in respect to growth. They point to other countries and say: See how fast they are growing in comparison with the United States? They point, for example, to Russia; and they point to Japan and to Western European countries. I think we must view these differences in rates of growth, which have been very real in the postwar period, in some perspective. The high rates of growth in countries like Japan, Western Europe and Soviet Russia in the postwar period reflect the recovery from the war when efficiency was very low, and from the immediate postwar period when efficiency was also very low. It would be natural, therefore, to expect that these countries couldn't sustain such high rates of growth in the future. Once they have recovered, that particular force making for high rates of growth will come to an end.

Q *This will be because they become beset by those competing elements that you spoke about?*

A That, of course, is in the picture. But I had in mind the fact that immediately after the war Germany, for example, had a big job of getting back into business. But she had people with ability and education. These are the important intangibles we were talking about. She had an industrial system of great power. But her output was very low. Then, as recovery set in, she put these people and their knowledge, and this system, to use. She was able to achieve a fast increase in output, which took the form of an increase in productivity. Obviously, however, once she is back on her feet, this particular source of growth comes to an end, and then the more normal factors take over. I think this can be said to apply to Western Europe, to Japan and to Soviet Russia, as well.

Q *What about the different techniques with which we and they measure growth?*

A In countries like Soviet Russia the rate of growth tends to be somewhat exaggerated, partly because of the way in which it is measured, partly also because Soviet Russia and others are at an early stage of their development relative to the United States. They are making use of knowledge and technologies that have been developed on the outside. As they exhaust the stock of unused knowledge, they will find that their rates of growth will begin to slow up a bit. It's a little like the postwar recovery kind of thing, except that it applies to a longer period of time. This is a difficult point to get across.

Hidden inefficiencies

Q *Soviet economists say that the real economic race begins once they have reached a level of development where they feel they have an adequate launching pad, so to speak. They say that it will be the efficiency of resource use that will make the difference, and that in this their system is clearly superior. We can only assume that they are putting a great deal of stock in their over-all planning. Could this be something that we ought to do some thinking about?*

A Oh, this is a very important, very vital question that confronts us here in the United States today and in other countries, as well. Is it true that a nationally planned, centrally organized economy like that of Soviet Russia must necessarily be more efficient than a free enterprise economy like that of the United States? I am not ready to say that that is the case. I feel that there are many inefficiencies in a centrally organized economy which are hidden, submerged but nevertheless are there—wastes of all kinds. And there are many efficiencies in a country like the United States which do not appear easily to the naked eye but are nevertheless there and operate.

Q *No system is perfect?*

A Of course not. Now, I don't mean to say that we cannot and should not improve the efficiency with which we advance productivity. I think there are many ways in which we could expand our productivity and growth. There are kinds of investment by government which would be desirable. If we look out the window here and watch the slow pace of the traffic up, down and across Madison Avenue, we see a most interesting example of inefficiency in the transportation of goods which is slowly choking this country. The suggestion has been made that there ought to be a new cabinet post to deal with urban and related problems. I think efficiency is to be sought there as well as in other ways. There

are real possibilities for improvement, and we need to take hold of them.

Q *What about other sources of improvement?*

A In addition to improving transportation within the urban areas, we need to do a real job in improving our interurban transport system. The inefficiencies that have crept into the railroads and other forms of transport because of inappropriate policy with regard to rates, regulations and so on are vital in this connection. I suspect that we can get substantial improvements in our national efficiency by revising our present transportation structure and our regulations of them. I would go further. We referred to the distressed areas before. The problem of the distressed areas is not only a problem of human need, a very real problem which deserves to be taken care of for its own sake, but there is a problem also of inefficiency. People are not being utilized properly to produce the goods and services that they and the rest of us want and need. Therefore, to solve the problem of distressed areas is to take care of that human need and also to increase efficiency. As I said, that can be done either by getting the people out of those areas or by moving industry to them—or some combination of the two. This is a very important problem that needs to be worked on.

Considerable government investment involved

Q *On this question of improving the quality of our resource allocation, to what extent might this involve some shift of resources from the private to the public sector of the economy?*

A I indicated a moment ago that there are some important ways in which you can have further government investment. For example, certainly a solution of the urban problem of transportation, housing and so on would involve a considerable amount of government investment. On the other hand, this does not mean that total government investment must necessarily increase, or increase more than private investment. There are some forms of government investment or government expenditure which I am sure could be found to be less than necessary, or certainly not as important as some other things that we want and need. Therefore, I would not argue that an increase in the total of government investment relative to GNP is essential. It might be, and it might not.

Q *In other words, the shape of government investment is what is important.*

A The shape, I think, is extremely important here, that's right. But on the allocation of resources, you're really raising another question as well—namely, the nature of the tax system. I think some of the inefficiencies of our present economy arise out of the inadequacies of our tax system. One of the things we're starting to do here at the National Bureau is a study of taxation and economic growth which will deal with some of these questions. Taxation is undoubtedly a powerful factor affecting not only the allocation of resources, but the incentives of businessmen, investors, savers and workers generally. Their incentives to work, their incentives to save, their incentives to invest and also the efficiency with which they do these things are involved. A complicated tax system, a high tax system and an unnecessarily high progressive rate, for example, could make businessmen spend an undue proportion of their time on ways of cutting taxes rather than on ways of cutting costs. Indeed, their major cost becomes the tax, and they spend their time on that rather than on seeking technological improvement. From a social point of view, business efforts to cut taxes yield no benefit. Business efforts to cut costs, to reduce labor requirements and to improve technology confer very great benefits on society at large. I don't think we ought to ignore things like that.

Providing incentive

Q *In what other ways can a greater efficiency in the use of capital be derived?*

A I think the function of an economist is not to point to particular ways of making improvements, but rather to point to ways of improving the environment so that investors, businessmen and others will have a very strong incentive to find such improvements. The economist's problem is not to indicate what new machine is needed, but to indicate how to put people in a position where they will want to look for new machines.

Q *What are the ingredients of an improved environment?*

A Taxes are certainly a major ingredient. I would add other things. For example, competition is an important ingredient. Competition within the United States makes for and puts pressure on people to look for better ways to do things—for new markets and new products. Competition between countries is also a good thing, and this is one reason why the national policy of the United States is in the direction of a freer world trading system. It is precisely in order to spread the benefits of competition that we want free trade among the countries of the world.

Q *On the question of research expenditures by companies, isn't there a problem in that companies cannot estimate in advance the returns of a given research investment, and yet this is the kind of investment that they will need more of? Isn't this an area where economists might eventually be able to contribute materially to general improvement in productivity and efficiency?*

A Well, I suppose that economists have a role to play in studying the effects of technological development on economic growth, on inventive activity, and the like. But it's a very difficult problem, and I don't think we'll ever be able, in a progressive society, to make precise estimates of returns from investments. Whether these be in research and development, or, indeed, tangible equipment, it's guesswork. The important thing is to put people in a position where they have an incentive to make such investments, where they have an incentive to expose themselves to the risks that are involved, risks

that may also yield a profit and lead to social benefit. I don't think economists can really do much on the question of making a better calculation.

Need to spread economic knowledge

Q *Dr. Fabricant, you've discussed a number of areas that may need some adjustment and further study. It occurs to me that the only real way a relatively free economy can make these adjustments with the least possible maladjustment is adequate knowledge. Since you are in an ideal position as a research director of a major research organization, what is your evaluation of how quickly economic knowledge is diffused in this type of society?*

A Well, we need not only to increase our economic knowledge, but we need to spread it around among the people. This is especially important in a democratic society in which, as we saw in our recent election, the man in the street has to make a decision on the vital economic issues. He needs to be informed reasonably well on what those issues are and what the consequences might be of a choice in one rather than another direction.

Q *In our kind of society, considerably more people do the resource allocating than in more centralized societies. Therefore, is it not true that the problem of diffusion of knowledge of all kinds, not only of economics, is much greater in a decentralized, consent society than in a centralized, authoritarian society.*

A Yes, I think that's fundamentally true. Freedom entails responsibility. One cannot be free without having responsibility to make decisions that affect oneself and one's neighbors. And one cannot be responsible without some degree of knowledge of the consequences of one's decisions. From that point of view, a free society must necessarily have a broader diffusion of knowledge, and not only of economic knowledge, than a slave society. The recognition that this was a fundamental factor in the growth and progress of this country underlay the decision to set up free public schools a century or more ago.

Q *Dr. Fabricant, I'd like to return to this problem of where our growth rate is going. The figure of five per cent has frequently been suggested as a desirable growth rate. But obviously problems will come up with any conscious attempt to push growth rates to five per cent. Is it possible to get five per cent? And if it is possible, is it desirable in view of problems that may arise?*

A Well, I think we ought to keep in mind the point that we discussed earlier. We tend to underestimate the rate of growth of this country, and I think also to underestimate the rate of growth of this country in relation to other countries. The quality factor alone surely would add significantly to the rate of growth that I mentioned before—three and one-half per cent over the last 60 to 70 years, and somewhat more than three per cent since World War I. I think the quality of products in this country has been improving, while in countries like Russia, for example, there is much less variety and quality. One reason they have been able to grow so rapidly is simply for that reason. If, as I suspect, the Russians try to do better by their consumers, introducing greater variety, better quality, more service at the distribution end, I think we'll find that their rate of growth will begin to look more like ours than it now does. Whether these corrections and prospective developments would be sufficient to put our rate on a par with theirs is very difficult to say. Nobody really knows.

Q *But you feel we can get a higher growth rate?*

A Yes. I've mentioned ways in which we can improve it. And we ought to work very vigorously on developing these ways of improving our rate of growth. I think if we can improve our incentive system, we can get more growth. Whether we can get five, six, or four and one-half per cent, or some other particular target, is a matter of guesswork. Nobody knows enough about the workings of this or other economies to guarantee anything. But it also depends, of course, on the price that we want to pay. I rather suspect that if we were willing to be ruthless with farmers and with people in distressed areas, if we moved them around the way slaves might be moved around, we might get some increase in our rate of growth. There's always this question of what you're willing to pay, and there's also a question of how much you really need to pay in order to meet the competition.

Q *Thank you, Dr. Fabricant.* ■

An End to Isolation

by FRANK A. TINKER

■ THE ARMAMENTS INDUSTRY has been with us since the first spears and coats of mail were fashioned. In modern society, however, this manufacturing complex has taken on intricate forms and is creating or making possible some highly unlikely communities. Many of these are totally creatures of the moment, such as the missile sites in Florida or the atomic testing grounds in Nevada and New Mexico. When the necessity for them ends, these settlements will disappear, since there was little activity in them in the past and no reason for them to continue. Few people will be affected by their going.

Other communities were well established before the economic stimulant of armaments. They were not created by the armaments industry, and they will have other reasons for continuing after the need for armaments passes or its nature alters. Their adjustment to the invasion is much more severe because they *do* have the philosophy, the expectancy and the background of permanency. Furthermore, their citizens *will* be affected if the defense industries pull out. Whether or not this will occur in any specific case is still speculative. Of more immediate concern is the impact of such an invasion upon a settled and abiding society.

One of the most remarkable examples has occurred in Utah. Isolation and lack of industrial plants had inevitably caused many of the Far Western communities to develop somewhat apart from the rest of the country. But, in addition, the peculiar history and outlook of Mormon society have tended to impart an even more insular character to the Utah valleys. The coming of an entire industry into this area might be expected to have revolutionary impact on the people's outlook.

The story of the withdrawal of the Latter Day Saints to Utah a little over a century ago is familiar. But it is less well known how thoroughly they cut themselves off from the rest of the country. It certainly has been impressed upon many travelers or would-be settlers in this socioreligious community that they were either out of place or simply unwanted, and that as recently as World War II. A schoolchild last year asked a newly arrived student if the people back East still thought Mormons wore horns and had many wives. This childish exaggeration reflected the residual attitude of proud separateness which has been common in Utah.

One of the most colorful chroniclers of Western America, Wallace Stegner, described the possible conquest of this attitude in his excellent book, *Mormon Country*: "But if the tourists ever discover in numbers the back country that lies behind the loop of national parks and monuments, if they ever by any chance get up on Thousand Lake Mountain or the Aquarius Plateau, if they ever make their way to the Grandaddy Lakes Basin in the Uintahs, if the promoters ever succeed in exploiting to the full the skiing at Alta . . . the valleys of the mountains are no longer going to provide sanctuary. The Gentile [non-Mormon] world, this time as tourists instead of miners or railroad men or cowpunchers or scientific explorers, is going to dilute Mormondom again, and from that dilution the separate and eccentric Mormon society may never emerge."

Mr. Stegner was only partly right. The skiers and tourists have indeed arrived in Utah during the past decade, but their influence has not been comparable to that of the wave of defense industries which swept over the state, nor has it lived up to his expectations.

At this point, it needs saying that Utah is only one example of a community whose character has been threatened by a defense invasion. Many other communities have had similar experiences. One of the most cherished traditions of America is its diversity; each region is proud of its own uniqueness. It is this hallowed personality, as well as the economic status quo, which is attacked by any flood of outsiders; and almost every region of the country has shown antagonism to large groups of newcomers for this reason. Utah is an extreme case only in that its history of isolation might be expected to intensify this antagonism.

Industrial Utah is made up of a single settlement lying along the western slopes of the Wasatch range, just east of the Great Salt Lake. This 75-mile-long development includes Salt Lake City, Ogden, Provo and Brigham City. In the past this has been the center of an economy

supported by agriculture, metals and transportation. The sugar-beet industry, developed and largely controlled by the Latter Day Saints Church, has provided a market for one of the major cash crops, and various vegetables are canned by large food-processing companies. Kennecott's copper mines at Bingham are among the world's largest, and the U.S. Steel Co.'s mill at Geneva ranks first in the West. Due to its location, this valley has been a historic hub of travel and transport, particularly for railways.

Self-sufficient community

Military organizations and contractors began to arrive in the Valley of the Saints shortly after World War II started. They came to take advantage of the local labor supply, to move from crowded and vulnerable coastal areas, to be nearer the metals mined and smelted in Utah and to make use of the state's unique distribution facilities. Into the midst of this self-sufficient community were suddenly thrown five huge military bases, one of which has had the largest single payroll in the state ever since. Moreover, unlike other wartime encampments, these were adaptable to peacetime—or, at least, cold war—use. When the shooting stopped, they scarcely paused in their growth.

Hill Air Force Base has now become one of the major supply and repair centers of the Air Materiel Command, having the prime responsibility for several missiles and aircraft. The Utah General Depot at Ogden is a storage and distribution hub for Army units in the 11 Western states, and the Naval Supply Depot at Clearfield performs much the same service for our Pacific fleet. West of Salt Lake City, the Dugway proving grounds is a center for testing and developing our chemical and bacteriological weapons and defenses. The Tooele Ordinance Depot restores and reconditions large quantities of military ammunition. On all these installations, by far the largest percentage of employees are civilian residents of the area.

With the dawn of the missile age, still another large boost was given to the valley's economy. During the last four years, four large companies have set up plants there, and one already established corporation was awarded a major contract. Sperry-Rand arrived in 1956 to work on intricate rocket systems and is now manufacturing the Sergeant missile. Thiokol and Marquardt followed in the next year with ramjets, solid fuels, and the Matador, Falcon and Nike-Hercules weapons. The Hercules Powder Co. was awarded a large Minuteman contract in 1959, and in 1960 the Boeing Aircraft Co. arrived to start work on a new facility at Hill AFB in which it will assemble the Minuteman missile.

Because of the myriad unlisted expenditures made by these companies and defense installations, it is almost impossible to measure their complete contribution to the local economy. Some basic figures provide more than a hint, however. Utah's total income from the sale of farm products in 1959 was $166 million. A single military installation, Hill AFB, spent more than half this amount, $96 million, in wages and local requisitions. There are only 19 employers in Utah with more than 500 workers; nine of these employers are engaged in defense work. The total nonfarm employee force is about 273,000 and one in 11 of these —25,000—is paid directly by the federal government for work on military installations. Over all, in 1959 nearly one-sixth of the state's total personal income came from defense; of the $1.6 billion earned, $250 million came from these expenditures.

This, of course, concerns mainly those persons working directly for the defense effort. It is difficult, however, to gainsay the indirect effect of defense spending. It is estimated that from 150 to 220 other citizens obtain a livelihood by furnishing services and goods to each 100 new workers in an area.

From this assumption it could be surmised that the 33,000 jobs given to Utah by the defense effort actually support a minimum of some 75,000 families—nearly a third of the state's population. But this does not take into account the number of wives who have gone to work because jobs are available, or the fact that many providers of goods and services who were already in business have expanded their operations and not given way to incoming competitors. On the other hand, the large percentage of metals and other goods produced in the state which wind up in the defense bins have not been counted either. In any case, it is clear that defense plays an inordinately important part in Utah's economic life.

Altered movement

In offering employment here for outsiders, or many persons who might otherwise not have stayed in the state, this new industry has already altered the traditional movement of population. Since the state still ranks 32nd in the U.S. in per capita income, even a small addition to income would prove critical for many persons. But there was no such trifling addition. Between 1954 and 1959 the average U.S. citizen increased his income by 33 per cent; along Utah's Wasatch front this gain was more than 44 per cent.

Prior to World War II, there was marked emigration from the valleys of Zion because of a high birth rate (about one-third above the national average) and insufficient local opportunities to sustain the resultant growth. With the beginning of the 1940s, however, this trend was reversed, and today there is a net inflow of young families amounting to approximately 40,000 persons over the last decade. This influx and the retention of those who reached ma-

turity increased Utah's work force by 22 per cent between 1950 and 1959. Only eight other states bettered this figure.

Probably the most noticeable effect of Utah's defense gains has been the almost complete urbanization of the population. This, in an area so vast and historically devoted to the good moral influence of agriculture, is a transformation indeed. Although the total population increased by 28 per cent, 13 of Utah's 29 counties lost population during the last decade. Over *three-fourths* of the state's citizens now dwell in its single metropolitan strip. More than 550,000 of Utah's 880,000 people live in just three of the metropolitan counties. One of them, Salt Lake, has added nearly 40 per cent to its rolls during this period.

Urbanization is a national trend that, in Utah, is accentuated by defense work. As far as the practical Utahan is concerned, this work is as good as any other, and he is usually happy to see it arrive, whatever the accompanying difficulties. Further, he almost desperately wants to be assured that it will not depart. One of the best ways to start an argument in this area is by remarking that these industries are temporary by their very nature and will eventually give way to other means of defense or even be eliminated by a disarmament program.

Concern for jobs

A Member of Congress from Utah who believed that the Bomarc system was outmoded and less effective than others committed the grave political error of voting against funds for its continued development and manufacture. Unfortunately for him, the Bomarc installation at Hill AFB employed many of his constituents, who made it clear that their prime concern was for their jobs rather than for the best defensive weapon available. Another congressman claimed as a campaign coup that his influence with committee chairmen was the reason the Bomarc program was reinstituted and the cutback avoided.

In spite of such political maneuverings it remains true that armaments must be considered as extremely variable, particularly during the present era of technological improvement in missiles and their component systems. While the defense industry as a whole undoubtedly will continue to be an important part of the national employment picture for some time to come, its increasingly specialized nature may encourage or even require its frequent geographic dislocation as emphasis is shifted from one weapon to another. Utah's unique community has apparently enticed a visitor who, although wealthy, is even more fickle than his ancestors.

Nevertheless, through the Utahans' desire to retain this affluent tenant, the political nature at least of the Mormon society might be expected to alter. It is certain from the single Bomarc incident that a large number of Utah's workers would be cool toward any programs of disarmament, and understandably so. In the event any sudden decision is made to reduce expenditures, either on over-all defense, or on a particular missile or service provided locally, a near crisis might strike those residents who had bought homes, cars and all the paraphernalia of well-being. There is simply no alternative employment in the state for the large percentage of the population now supported either directly or indirectly by military expenditures.

In a somewhat similar area, Southern California, a survey made several years ago showed that the younger persons living in the boom atmosphere of that gilded valley simply could not believe that the federal government would let the bubble burst. They felt that somehow it had become the responsibility of the government not merely to provide relief and opportunity, but to maintain the economy at the inflated level to which they had become accustomed.

Utahans have not been unusually individualistic by nature, since the idea of community was stressed strongly by the church and the pioneer tradition; but they have looked inward to that community for help in time of need rather than outward to a federal program. How their attitude toward federal encroachment and their own community may change when the new prosperity is threatened remains to be seen. With a somewhat stauncher background of self-reliance, the Utahan may not turn so completely and trustingly to governmental dependence as the Californian. In the meantime, one thing is certain: he is much more interested now in the affairs of his nation, and this cannot help but alter his outlook to some degree.

Halt in emigration

Has the arrival of defense industries brought about great changes in the Mormon character and society? As yet, no such conclusion is warranted. For one thing, much of the growth in population resulted from a halt in emigration. In addition, the pull of this society upon its departed members is very strong. Several of the new companies found that a large percentage of their employees were former Utahans, encouraged to come home by the prospect of employment.

This is not an entirely local phenomenon. The "Okies" who fled to the milk and honey of California returned to the dusty flatlands as soon as there was an economic reason for the move. Indeed, though almost any uprooted citizen of our increasingly fluid society may go wherever there are good prospects of employment, he will go most willingly to his former home.

At present, only the *structure* of the community in Utah has been

seriously altered by the coming of the defense dollar. Mainly, this has amounted to an increased concentration of the population, with all the attendant responsibility and difficulties being placed on the metropolitan areas and their government.

The *individual,* under the presumably "leavening influence" of new arrivals, has not shown many signs of experiencing a revolutionary change of attitude. He has certainly gained a new interest in national and international affairs, but, so far, only to the extent that they affect his pocketbook. He is most apt to consider these momentous affairs from the same provincial standpoint he cherished previously, and possibly from an even more self-centered attitude than he showed before his income became so dependent upon continued conflict. In other areas, such persons have gradually become more prone to rely on federal programs of aid, such as that proposed now for education. Over all, the "government dollar" loses some of the taint it may have had.

As yet, few communities such as that in Utah have been deserted by their generous, demanding tenant. Defense, as it is being managed today, incorporates its activities into the basic economic life of the region and is an entirely new factor. What changes it has brought seem to be confined to the mechanical operation of the host society. Whatever permanent change modern defense spending manages to effect in the individual will have to wait to be proved until that spending has ceased. At present, these alterations are superficial and quite likely to be as transient as the coin that caused them. ■

Realities in Search of a Theory—No. 5

Public OR Private: *Where's the Line?*

by ROBERT LEKACHMAN

Fifth in a series of articles dealing with the lag between the way we think our economy behaves and the way it actually does behave.

■ WHEN ADAM SMITH WROTE *The Wealth of Nations* in the same miraculous year that the Declaration of Independence appeared he had few doubts about the desirable distinction between public and private activity. Defense, the exact administration of justice and the construction of a few essential public works, like roads and bridges, exhausted the agenda of government. For the rest, natural liberty demanded that businessmen compete freely among themselves for customers, and workers compete freely with each other for jobs.

Nor did Adam Smith consider it any disgrace for businessmen to single out profit as their primary objective, and for workers to aim at higher wages. Private selfishness was the means to public welfare, or, in Smith's words, "Every individual is continually exerting himself to find out the most advantageous employment for whatever capital he can command. It is his own advantage, indeed, and not that of the society, which he has in view. But the study of his own advantage naturally, or rather necessarily, leads him to prefer that employment which is most advantageous to the society."

Smith's certainty did not survive even the 19th century. Almost at the century's beginning, English governments began to question whether unchecked competition was, in every respect and in every place, "most advantageous to the society." The first hesitant intervention on behalf of child workers was soon followed by other factory acts which applied initially to women and ultimately to adult male workers as well. These laws recognized English society's inevitable interest in worker welfare and its swelling doubt that competition alone would adequately protect it.

By the middle of the 19th century, John Stuart Mill, while clinging to the general principle of *laissez faire,* found himself forced to identify a growing list of exceptions to it. As the century waned, the flood tide of Victorian reform and Fabian socialism increasingly blurred the clear distinction between public and private which the classical economists had labored hard to draw.

In the middle of the 20th century the problem has become a great deal harder, and classification much more difficult. Our society and its institutions are fantastic in size and complexity. New institutional forms have proliferated. Relations between governments and private organizations have changed. Even traditional institutions have been forced to reinterpret their appropriate functions. Let us consider in detail some of these changes.

In much of American manufacturing the economies of scale have proved so substantial that very large units are frequently the only really efficient ones. Recent Senate hearings conducted by Sen. Kefauver concluded that minimum economical size for an auto assembly plant demanded a yearly output of 300,000 to 500,000 units. It is not astonishing, therefore, that American Motors, although only the fourth largest auto manufacturer, is one of the nation's 100 largest manufacturing organizations.

To take another instance, erection of a modern steel mill demands perhaps half a billion dollars in capital. It is difficult for anyone to regard

with benevolent indifference the activities of these corporate behemoths, in the secure confidence that whatever they do will all work out for the public good.

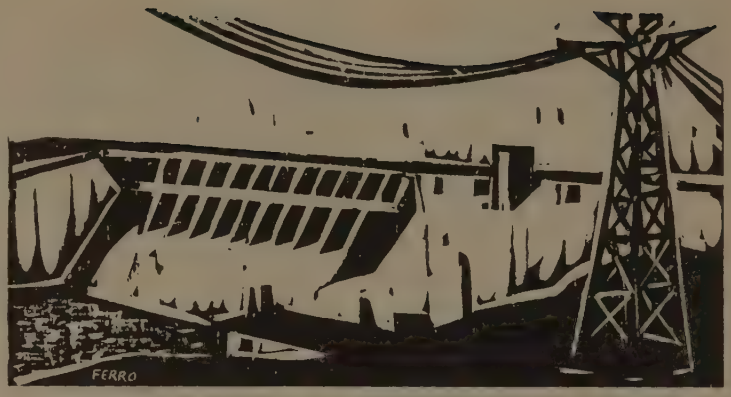
Small adjustments by small units no doubt cause only minor disturbances of employment, income and output. But the same is not true of large units. In an important sense, Charles Wilson was right when he made his famous identification of General Motors and the public good. For if General Motors were to lose its wonted efficiency, the result could scarcely fail to be a national disaster. If other countries began to supply the bulk of the American automobile market, unemployment, shrunken sales and reduced incomes would make it abundantly clear that the fate of General Motors interested many more people than General Motors stockholders and employees —themselves a large army.

Intense debate

In a number of ways, the private activities of the large corporations are of inevitable public concern. They may impinge on foreign policy and the American image abroad. A recent instance is the Ford Motor Co. decision to enlarge its majority interest in its British subsidiary to total ownership. Ford's offer of more than $300 million for the minority holdings touched off an intense debate among Englishmen over the propriety of the action. At a time when the delicate matter of a Scottish base for our atomic submarines was also at issue, the Conservative government found itself involved in parliamentary explanations to the Labor opposition.

Again, our large oil companies are unavoidably involved in the tangled net of Middle Eastern diplomacy. At key points both these companies and our government have recognized the practical necessities of coordination. In Latin America, the policies of the United Fruit Co. have frequently had as much to do with Central American attitudes toward the United States as the efforts of our diplomatic representatives.

None of this implies that our government and our large companies regard themselves as allies, or that either accepts the dictation of the other. But it does show that when



an American company conducts large operations abroad, its policies inevitably influence foreign opinion. This results in occasional tangles. For example, Aramco has refused to hire American Jews out of deference to the prejudices of its Arabian hosts. No doubt this action eased our diplomatic relations in an explosive region, but equally certainly it offended American sensibilities.

Foreign policy is only one illustration. Our domestic statutes recognize at least one area where the private actions of American industry vitally affect the public interest. This is labor policy. The injunction procedure established only 15 years ago by the Taft-Hartley Act recognized that there are circumstances which render work stoppages dangerous to the national health and welfare. Our practice corroborates our statutes.

Personal intervention

Eighteen months ago Vice President Nixon and Secretary of Labor Mitchell ended the 116-day steel strike by personally intervening between the disputants. They could scarcely have demonstrated more conclusively their conviction that what happens in the steel industry far transcends the private interests of the original parties to the argument.

Corporate policy on the location of industry is also touched with the public interest. To individual communities it makes an enormous difference whether large companies open new branches or close old ones. In one of his business novels, *Sincerely, Willis Wayde,* the late J. P. Marquand centered the ethical interest of his story on the responsibility of his hero. Was it to the small community whose prosperity rested upon the belt factory then in operation there, or was it to the large company which employed him and expected him to locate plants where economic efficiency dictated?

These are questions which corporations as well as novelists are beginning to ask. Some corporations have answered by deciding to locate in communities which would not be wholly dependent upon them. Such a decision surely compromises with the single imperative of profit maximization.

Hiring and property management also have public connotations. We no longer, as a society, seem quite willing to accept the businessman's plea that his interest is only in commerce and profit, and that social policy is none of his concern as a businessman. Instead, we tend to demand that he conform to certain public criteria of nondiscrimination in his hiring. It was not long ago that the New York State Commission Against Discrimination persuaded an airline to hire Negro stewardesses. Court action directed the Metropolitan Life Insurance Co. to accept Negro tenants in its housing developments.

Common thread

There is a common thread running through these varied instances. As a society we have apparently concluded that our business organizations are sufficiently large and influential to have to conform, in some respects at least, to commonly accepted public canons of behavior. Such is the very considerable meas-

ure in which we have departed from the 19th century's reluctant acceptance of responsibility for plant safety, hours of employment and working conditions.

At no time in our history were the lines between private activity and public participation sharply drawn. In the 19th century we subsidized canals and railroads, not to mention farmers and college students. By the end of the century we were willing to draw the logical conclusion, embodied in the Interstate Commerce Act of 1887, that railroads were at least quasi-public institutions, legally subject to community regulation. The new instrumentality was the regulatory agency.

This century's inventions are far more numerous. The Federal Reserve Act of 1913 deliberately established an anomalous, mixed system of central banking. The Federal Reserve banks no doubt are owned by the participating commercial banks. Yet the President appoints the Board of Governors which administers the system. The stated objectives of the system do not include private profits and, in fact, the law limits the earnings in which the commercial banks can expect to participate. The Hoover Administration's Reconstruction Finance Corporation represented another social invention, this time in the shape of a government-financed lending institution, directed to conduct its affairs after banking models.

The New Deal, of course, spawned a veritable school of public financial institutions which operated in fields previously the preserves of private institutions. The Home Owners' Loan Corporation engaged in a mass mortgage rescue program. Ultimately, it wound up its affairs with a small profit. The Commodity Credit Corporation has acquired title to monstrous supplies of grain, cotton, tobacco and other farm commodities. If it ever breaks even, a modern miracle will have taken place. The Federal Housing Administration guarantees the loans which private institutions make.

Secondary mortgage market

The Federal Deposit Insurance Corporation insures savings deposits in private banks, and savings and loan associations, up to $10,000 per depositor. The Federal National Mortgage Administration, "Fannie Mae," has established a strong secondary mortgage market. Through the years, the Rural Electrification Administration has aided the spread of electricity by loans to rural cooperatives.

In one or more attributes at least, each of these institutions is a monument to our social ingenuity. In some respects these agencies are private operations. They extend credit to individuals or to organizations which would otherwise have sought private funds; or they issue securities in the capital market after the fashion of the large private corporation; or they operate under an in-

junction to break even; or they combine these attributes. Thus, these agencies supplement, influence and support private credit instrumentalities.

Undoubtedly these governmental inventions have altered the conditions under which American business and industry operate. Nevertheless, it is a question whether, especially since the end of World War II, they are as important as private institutional innovations. The pension fund, the mutual fund and the foundation are three examples of new or evolving institutions which differ significantly from traditional private enterprise, and have not yet had applied to them commonly accepted canons of public supervision.

In some ways the foundation is the simplest of these forms. Private inspiration is basic to its creation. Yet the foundation is legally separated from other private agencies. We formally endorse its nonprofit character by the grant of tax exemption. This extremely valuable privilege carries with it the obligation to support activities which benefit the community. The enormous range of foundation concerns testifies to the charitable, educational, humanitarian or cultural projects which satisfy this criterion.

The Rockefeller Foundation, the oldest of the important foundations, has traditionally supported medical education and medical research. The newest of the giants, the Ford Foundation, has taken to its heart educational experiment and social science research. For decades the Guggenheim Foundation has aided talented individuals to travel, write, paint, sculpt and experiment. The Rockefeller Brothers Fund has invested directly in promising small businesses which lacked alternative financing. A number of foundations, including the Mellon Institute of Technology, the Armour Institute, the Southern Research Institute and the Midwest Research Institute of Kansas City, have endeavored to develop new products or processes for license to private enterprise.

Spectrum of activity

Through the foundations, the community participates in a wide spectrum of activity; some supplement private business and others relieve government of parts of its burdens. As an institution, the foundation represents a merger of private and public purpose. A recent example of the ambiguities its double identity sometimes causes occurred during the recent Presidential campaign. The Kennedy Foundation, supported by the new President's family, was engaged in a contest with the State Department over the issue of travel aid to African students who were planning to study in the United States. More or less inevitably, the foundation finds itself, at one end of the range of its activities, close to the private business and, at the other end, entangled in quasi-governmental tasks.

Pension funds represent another institutional development. Some of these funds are managed by trade unions, some by employers and most by a combination of both. Financing arrangements vary still more widely. The pension fund, too, is an unusual private organization. It is designed to produce welfare rather than to maximize profit. Prudent fund managers therefore concentrate on securing a stable level of benefit to union members rather than a high rate of return on investments.

So clearly do pension funds resemble the welfare features of modern government that we have begun to supervise them in the public interest. Congress took the first timid step in this direction when it passed the Welfare and Pension Funds Disclosure Act of 1958 which requires annual reports on fund operations. Moreover, these funds have grown to tremendous size; in some cases they come close to controlling the companies which created them. The Sears Roebuck Fund is the largest single holder of Sears Roebuck voting stock. Since other stockholders are scattered, the managers of the fund could, in theory, replace the managers of the company.

Relevant point

This last point is particularly relevant to the mutual investment funds and their older brothers, the trust funds. As Adolf Berle has recently pointed out in *Power Without Property*, the bulk of American trust monies are administered by a dozen or so major New York City banks and about the same number of large insurance companies. In his opinion, the men who administer these funds are "essentially, non-Statist civil servants" who are not tied to their enterprises by any relation of ownership. What is true of them is apparently beginning to be true also of the mutual investment funds.

The investor in one of these funds purchases his units at a given market value and is privileged to sell at any time at a price which represents his share of the market value of the securities the trust has acquired. But, unlike a true owner, he cannot alter the management of the trust. Paradoxically, the managers of the mutual funds characteristically refrain from wielding the vast influence which their tremendous holdings have created. They intervene in no arguments over managerial control of the companies in which they invest; much less do they start such contests themselves. When they are dissatisfied with a company's management, their simple and usual remedy is gradually to dispose of their holdings.

What we encounter is a dilution of the meaning of the word "private"—a further blurring of the relations between ownership, management and control. It is no longer a matter of managements running corporations which they do not own. We have moved to the point where owners do not even directly acquire their ownership interest. Professional managers of money deal with professional managers of enterprises. Only self-restraint on both sides and, perhaps, the force of habit have concealed the real shifts of power that are occurring.

Nineteenth-century economists could scarcely have imagined the snapping of the link between ownership and management, between investment and control, which these new economic forms signify. And, inevitably, public policy once again faces the delicate problem of supervising institutions which are not public, and yet are private in new ways which appear to demand clear public criteria as guides.

Evoke responses

Much of the preceding discussion has touched on the relation between government and private organizations. We have seen that new economic forms inevitably evoke governmental responses. But this is far from the end of the story. The government has initiated as well as reacted. Defense production is one of the most important areas in which government action has altered an older dividing line between public and private activity. It is an open question whether a firm like the Martin Co., which does 99.2 per cent of its business with the government, can be considered a private enterprise in any old sense of the term.

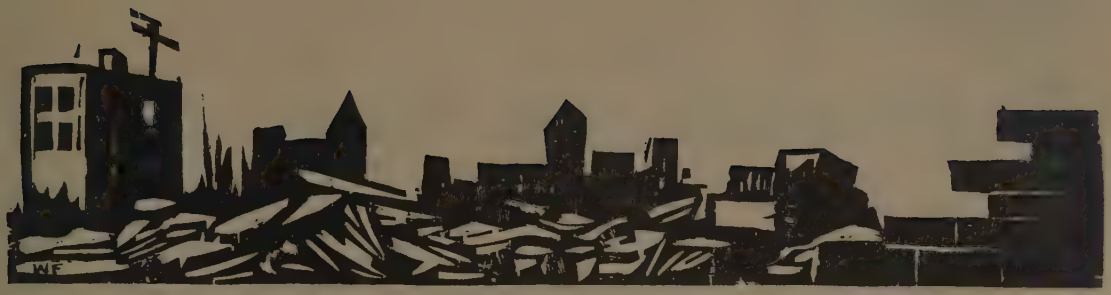
The size of its expenditures on plant and equipment are determined by the defense agencies. Its ultimate profits depend on the volume of government orders, the permitted rate of depreciation and the contractual arrangements offered. Indeed, this company and other major defense suppliers are so much identified in practice as an arm of the government that their employees must meet security and loyalty standards similar to those applied to civil servants. When government influences capital investment, profit rates, output composition and hiring practices, one must wonder whether a real line between public and private activity remains.

The government's role has also altered and expanded in relation to the universities. The defense agencies in particular have found it increasingly convenient to subsidize scientific research in the universities. Anyone acquainted with the physics or the mathematics department of a leading university can readily testify what this has meant. New laboratories and new scientific projects increasingly draw their support from Navy, Army or Air Force contracts. Larger and larger percentages of university scientific staffs spend all or most of their time on these projects.

Hierarchy of prestige

The conception of the university as a place where the faculty combines teaching and research is beginning to yield, in the scientific departments, to a rather different division of labor. Some of the faculty do the bulk of the teaching and rank lowest in the hierarchy of prestige. Others are essentially government scientific employees, paid by defense appropriations, and using government-purchased facilities. Since the research contracts include allowances for university overhead, the universities find themselves depending to an increasing extent upon government support.

Now none of these developments implies any wish on the part of the government to control the universities or any quest by them for complete federal financial support. Nevertheless, the meaning of the new relationship is already visible in some aspects of educational policy. The National Defense Education Act requires the recipients of its benefits to take a loyalty oath and to swear to an affidavit, both designed to establish their ideological cleanliness. Once again government



benefit has brought governmental criteria of employment in its train.

In the RAND Corporation, the Air Force has created its own private research agency. The scholars, technicians and scientists who pool their efforts in the idyllic climate of Southern California in many instances pursue private projects with military overtones. Much of the social science research sponsored by RAND is of general interest and wins general publication. Thus, while the universities have, in some instances, assumed certain military overtones, this military organization has taken on a fair number of academic stigmata.

By now the business corporation and the trade union are elderly institutions. But it is evident that these old dogs have learned new tricks and new roles. Take first the corporation. Gradually, and possibly reluctantly, the public utility concept is winning business acceptance far past the frontiers of telephones and power stations. Public utilities companies have long accepted rate regulation in exchange for market protection. Slowly, the leaders of other industries, while stopping far short of this proposition, are admitting that their price and output policies concern the public.

Steel is a good example. Since the end of World War II, the steel companies have raised prices many times —in all, 90 per cent since 1947, or more than twice the increase in manufactures in general. But in recent years they have taken care to prepare the way for public acceptance of these increases. In so doing, they have tacitly admitted the right of the public to a concern about their policies. It was part of the steel industry's case in the 1959 strike that union demands for increases could not be met because steel prices would inevitably rise and with them the general price level.

In the judgment of the steel companies, the fight against inflation demanded that both steel wages and steel prices remain steady. This, of course, is only another way of stating that the large companies of this fiercely private industry are showing signs of a new conviction—that they bear a special responsibility for the general economic health of the nation.

Companies in growing numbers are finding that they have a special interest in the vital public matter of education. It is only in the last 10 years or so that the courts have finally ruled that corporations can legally use profits to support educational programs. Corporate scholarship gifts, construction awards and general educational help have been steadily expanding. So has the corporate contribution to community charities. This is yet another demonstration that the ambit of corporate action has considerably widened since the old days when the single-minded quest for profit best described the behavior both of individual entrepreneurs and corporate managers.

Corporate ethic

There are occasional parallels to this whole shift of the corporate ethic in trade union behavior. The United Automobile Workers has taken the pioneer step of subjecting its internal decisions to examination by an independent Public Review Board. It is difficult to conceive of a clearer admission that a union is more than the economic agent of its members.

Unions, too, have discovered that it is expedient or wise to defend their actions as conducive to the public interest. Frequently it is remarked that the public is helpless when the great economic giants—unions and companies—lock in epic combat. It might be more accurate to note how aware both combatants are of the impact of their policies upon the community and how eager they are to justify their policies to that community. Implicit in these attitudes is acceptance of the community's right to judge private actions.

What are we to infer from this recital of some of the ways in which government and private agencies appear to be mingling their functions, assuming each other's characteristics, or creating new instrumentalities to accomplish new or old functions? One conclusion is safe. Changes in our institutional life have outrun our present classifications. Neither government, nor corporation, nor union nor university behaves quite as the labels suggest. And there are comparatively new organizations to which no existing label applies.

This tentative survey suggests two additional conclusions. One is that citizens in more and more activities are recognizing the public connotations of private acts. This recognition need not be the prelude to increased government control. It may, on the contrary, be the best hope of avoiding such control.

The last conclusion is also optimistic. The flexibility of our old institutions and our ability to invent new ones show the vitality of our society. We are refusing to allow old forms to inhibit new activities. Among animals, mongrel strains are the sturdiest. It may also be that mixed economies are the most viable. ■

An Effective Way to Settle Wage Disputes?

by A. H. RASKIN

■ IS THE DAY APPROACHING when collective bargaining on wages in major industries will be so governed by mathematical formulas that electronic machines will be qualified to do the negotiating? Will the rates of pay in steel in 1965 or 1970 be the product of an IBM computer standing in for David J. McDonald on the union side of the bargaining table and a Sperry-Rand Univac replacing R. Conrad Cooper on the management side?

The probability is that we will never reach such a mathematical exactness in our calculation of what constitutes a fair hour's pay that automation will rule the negotiating process as well as the factory. But there is strong evidence that we are moving toward an increasingly mechanical standard of measurement for the contract gains unions can expect to win for their members in most key industries.

The surprise has gone out of collective bargaining. In the pattern-setting industries like steel, automobiles and electrical manufacturing, the package value of the wage and fringe improvements in each year is predictable, within a penny or two, even before the parties start talking. The annual increases are likely to range from seven to 10 cents an hour, with little regard for whether business is good or bad, whether the union strikes or keeps its members on the job.

A complex of factors accounts for this shift away from the grab-bag type of bargaining that prevailed in most of the 15 years since World War II. The reduced effectiveness of the strike weapon, demonstrated with greatest force in the abortive strike against General Electric last October, is part of the explanation. So is the increased pressure of foreign competition and the great excess of productive capacity in most basic industries. But perhaps the most fundamental factor is the knowledge on both sides of the conference table that consumers—and their representatives in the White House and Congress—are unwilling to keep paying the bill for wage increases that are followed by price increases.

This is not the place to reventilate the debate over the extent to which the role of wages in inflation has been exaggerated or industry has unjustly used higher wages as an excuse for higher profits. What is important for this discussion is that the public has grown so resistant to the tandem relationship of wages and prices that unions and employers no longer can make settlements with the expectation that the customers will pick up the tab in the form of higher prices.

Rules—not money

This was the one clear moral that emerged from the 1959 steel dispute. Indeed, if wages were the sole issue, there would have been no 116-day strike. Steel management's attempt to change the established work rules torpedoed what otherwise would have been an almost certainly peaceful acceptance by the union of modest wage increases. The long walkout brought the union a victory on the rules, but not on the money end of the settlement. That stayed within the bounds of what the industry knew it could give without raising prices.

The replacement of President Eisenhower by President Kennedy is going to mean many changes in the labor-management climate, but the White House is not likely to become more indulgent of inflationary wage agreements. The new President and his Secretary of Labor, Arthur J. Goldberg, can be expected to devote ardor and an uncommon measure of skill to maintaining both peace and price stability on the labor front.

The net effect will be an intensification of the trend toward linking wage increases with increases in productivity. This, in turn, means more reliance on formulas for determining how much money should go into pay envelopes.

The big headache comes in deciding what ought to go into the formula. Economists for labor, industry and the government agree that higher productivity is the essential ingredient in a higher standard of living, but they differ on how productivity should be measured, and on how its fruits should be shared among workers, owners and consumers.

The traditional preference among employers has been for productivity wage systems geared to the individual performance of the worker or the work unit to which he belongs. This is the old piecework or incentive pay plan, still in wide use in the needle trades, steel and other large industries. Unions have disliked it, considering it a device through which management bribed workers to compete with one another to their own detriment.

Management helped discredit the system in many companies by pushing up the performance standards whenever the lure of incentive pay brought a general rise in productivity. The resulting "speed-up" was the chief force causing the rise of such unions as the United Automobile Workers. It incorporated in its constitution a prohibition against writing contracts that authorized individual incentive schedules.

The late Philip Murray, as President of the United Steelworkers, tried hard to persuade his locals to renounce incentive earnings in the steel mills. He argued that their principal effect was to make men

work themselves out of a job by producing more without an improvement in technology. But the extra pay had more weight with the union members than Murray's arguments.

One reason for this was that the companies in steel and other industries using productivity premiums stopped jacking up the output requirement whenever the bulk of the workers exceeded the norm. The companies wrote into their union contracts a guarantee that the standards would not change except where new machinery, materials or other external factors created a new physical condition influencing the work. The fear that the freer hand sought by the steel producers in 1959 would wipe out these protected work practices and standards was a primary explanation of the steel strike.

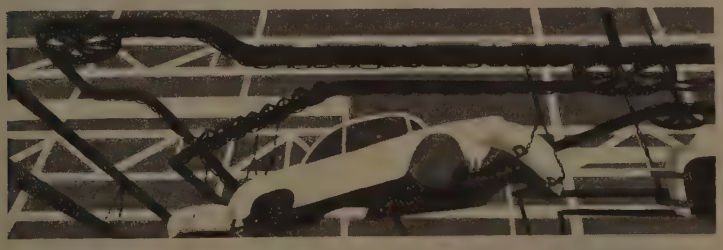
The real turning point toward union cordiality to a productivity wage formula came in 1948 when General Motors introduced its "progress-sharing" plan. The program has proved both the most durable and most copied in any basic industry. It originated with management, but its strongest backing now comes from labor.

The novel feature of the GM formula was that it provided for an annual improvement in the workers' purchasing power designed to reflect the over-all long-term improvement in the productivity of the whole economy. It discarded the individual's own performance, or even the success of General Motors in pushing up its corporate output, as the proper measuring rod. Instead, it relied on the doctrine that the worker was entitled to an equitable share of the increase in the real value of the gross national product in the computation of his basic hourly pay.

The formula had two parts. One was the guaranteed annual improvement in basic wages; the other was an escalator clause to offset changes in the cost of living. The initial improvement allowance was three cents an hour; in the present agreement, which expires on August 31, this annual figure has risen to six cents, or 2.5 per cent, whichever is greater. The cumulative additions to individual pay under the escalator clause have brought the workers 54 cents an hour more since the first pact 13 years ago. All but 17 cents of this has been frozen into base pay.

The auto union signed a two-year agreement in 1948 embodying the plan. The annual improvement feature intrigued Walter P. Reuther, the union's president, from the first. He joined the company in writing into the agreement a declaration that "to produce more with the same amount of human effort is a sound economic and social objective." This was the first affirmative recognition in the mass production industries that workers as well as management had a stake in the introduction of labor-saving machinery.

The part of the formula that gave the union the most unhappiness in the initial period was the cost-of-living escalator. Labor historically had been opposed to any "accordion" plan, under which wage increases could be taken away. When the upward surge of prices began reversing itself in the 1949 recession, John L. Lewis and other union leaders were intensely critical of the GM plan, and Reuther himself expressed a determination to bar its renewal. In steel, it was not until 1956 that the United Steelworkers would accept an escalator in its long-term contract.



By 1959, however, the steelworkers had found the escalator so advantageous that they fought hard but unsuccessfully to retain its full protection in their present agreement. The industry, on the other hand, turned against the clause on the ground that it helped feed inflation instead of combating it. It had added 17 cents an hour to steel wages in the three years of the 1956 pact.

The new agreement provided for a drastically revised escalator. It set a ceiling of six cents an hour on the escalator increases the workers could get during the full life of the agreement. It also provided that all or part of this increase could be wiped out if the cost to the employers for hospitalization and other social insurance went up.

In other industries that have adopted it, the gearing of wages to the rise and fall of the federal Consumer Price Index has been scrapped. Both the railroads and the electrical manufacturers no longer have such clauses in their contracts. Employers in other industries are bent on getting rid of the cost-of-living tie. Reuther already has served notice on the Big Three auto manufacturers that the UAW will battle against any tampering with either the escalator or the annual improvement feature of the GM formula in the Detroit negotiations this fall.

Substantial concessions

One reason why the auto industry is less enthusiastic than the union about the formula that management spawned is that the UAW has never regarded the combined fruits of the escalator and the annual improvement factor as all it is entitled to in economic benefits. Since 1950 Reuther has won other substantial concessions for automobile workers.

This elasticity in application of the formula has brought its effectiveness into question among industrialists. They feel its accent on the long-haul increase in the total economy, as against a focus on the record of the particular industry or company, removes any spur to greater output by a company's own employees and gives them only the slightest incentive to welcome automation or other technological improvements in their plant. Its chief effect, as these critics see it, is to saddle the employer with the responsibility for raising wages, under all circumstances.

Many labor and neutral economists also have reservations about the design of the GM formula. Labor hopes the Kennedy Administration will succeed in the next few years in

pushing the rate of national economic growth up to five per cent. Most unionists are convinced that an increase of only half that much in workers' purchasing power will hold back the country's progress toward faster growth by creating an even wider gap than now exists between our ability to make goods and our ability to sell them.

Weights and measures

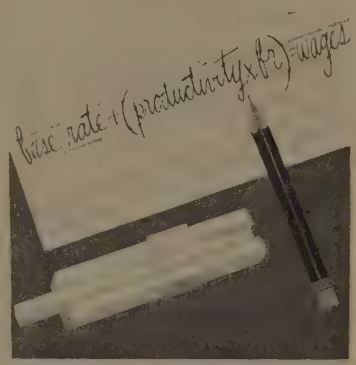
This leads to the real difficulty in trying to devise any acceptable formula to measure productivity. The formula itself will affect the way in which the benefits of productivity are allocated. What do you measure and what weight do you assign to each component to assure equity and encourage greater growth in the interest of the total economy?

The simplest yardstick, and the one labor likes best, is to use man-hours of work by production and maintenance employees. However, most experts are convinced that no worthwhile estimate of productivity can be made merely by dividing the number of units produced by the number of blue-collar hours worked.

Such an index takes no account of the steady shift in the production process from hourly rated to salaried workers—engineers, technicians, executives, clerks. The ratio of workers in this group has doubled or tripled in some industries in the postwar period, yet they are rarely counted in productivity computations. Other factors are even harder to measure. Billions of dollars are invested each year in automation, expansion and renovation, with the cardinal purpose of reducing manpower needs and thus heightening efficiency. Inventive and managerial skill, the impact of changes in raw materials and in product design—all these and a host of other factors deserve consideration in trying to work out a socially responsible productivity formula.

Even in a manufacturing industry, where some physical guideposts are available to provide a modicum of comparability, the task is complex enough to send an electronic brain to its automated psychiatrist. What measurements, then, would be workable in industries where service and skill are reflected in quality, rather than volume? And even when the measurements are devised, whose job will it be to remember that productivity can be a vehicle for giving lower prices to the consumer, not solely for raising wages and profits? As other countries pour more goods into our markets, this consideration will be increasingly important.

Perhaps the most ambitious attempt to establish a more satisfactory guide than is provided either by the GM formula or a man-hour productivity index is now under way at the Kaiser Steel Corp. There a tripartite committee is at work on what it hopes will prove a viable long-range plan for fostering technological progress and guaranteeing that the new wealth it creates will be justly shared among workers, stock-



holders and the community as represented by the buyers of steel.

The man who played the dominant role in creating the Kaiser committee has moved into a larger area of responsibility. He is the former general counsel of the steel union, now Secretary of Labor Goldberg. There is every reason to expect that he will seek to organize similar panels on a much broader basis in the hope that they will help labor and management in other major fields to agree on standards for determining future contract benefits without strikes.

Coordinated planning is needed at levels above the company or the industry, if we are to make maximum use of the beneficial aspects of science without producing extensive unemployment. This means that the government's role will largely be *to assist* in the gigantic task of retraining and job transfer that automation will make necessary.

All this indicates that we need not anticipate an atrophy of unions when and if there is substantial agreement on a broad formula for wage and benefit determination. The spotlight will move from the traditional concept of contract bargaining as an endeavor to be undertaken once every two, three or five years. Instead, there will be increased reliance on year-round joint discussions of mutual problems through established machinery.

It is doubtful that any wage formula will be sufficiently self-administering to permit the resolution of all disputes by computer, but it is inevitable that arbitrators or fact-finders will be used with much more frequency in arguments over what should go into new contracts.

There will be disagreement, for example, over when to reduce the basic workweek from the present 40-hour level—a disagreement that no formula can solve. It may be that the real showdown on this issue will come not at the bargaining table but in Congress through efforts to reduce the statutory ceiling on straight-time hours. In general, it is likely that the formula approach in wages will bring more peace in industrial establishments and a shift in the area of conflict from the picket line to the legislative hall.

But even this is not sure. If foreign competition becomes as bothersome an issue in all industries as it now is in a few, management and labor can be expected to join in an appeal to government agencies for protective measures. This could lead to a partnership so extensive on both the political and economic fronts that our worry might become the necessity for imposing restraints on too much harmony—cooperation carried to the point where it conflicted with the determination of sound public policy.

One dividend that can be expected to accompany the emergence of predictable wage patterns based on long-range formulas is that unions will be obliged to increase their interest in community betterment as a means of holding the allegiance of their members. Otherwise their organizations are likely to collapse as a result of dry rot. It is in this direction that much of the future of unionism will lie. ■

SPOTLIGHT ON THE SALESMAN

by RICHARD WADDELL

■ EVERY TIME the U.S. economy takes one of its periodic dips, we hear about the lack of old-fashioned salesmanship. We hear that automobile salesmen are order takers instead of creative salesmen; that clerks are rude and ill-trained in department stores; that Americans have lost the art of "putting the sizzle in the steak."

Certainly some of these charges are true. Actually, however, salesmanship—the personal closing of a sale—is more likely to lack zip when times are good. When competition gets rough, as it is right at the moment, evidence shows that salesmanship comes back into its own.

Just what has been the role of personal salesmanship—as distinguished from other types of selling such as advertising and direct mail promotions—in the postwar U.S. economy? Did personal salesmanship have anything much to do with the postwar boom? Or did Americans reach the standard of living they enjoy today by some other means? What of the future? Are salesmen going to be replaced by some automatic merchandising system?

It isn't possible to find clear-cut answers to these questions. But some useful analysis is indeed possible. Since 1945 the annual gross national product (measured in constant 1954 dollars) has almost doubled—from $318.1 billion to well over $500 billion. Personal consumption expenditures, too (again measured in constant dollars), have almost doubled—from $171 billion in 1945 to about $328 billion in 1960. The past decade has been called one of the greatest spending decades on record.

American businessmen naturally take pride in this record; it has been a vindication, after the dreary years of the Great Depression, of the free enterprise system. But if one probes into available statistics, one discovers that supersalesmanship, as personified by the dogged, sample-carrying peddler tramping the streets, hasn't played much of a role in bringing about this spending boom. At least, not up to now.

Let's try and justify that statement. The Census Bureau classifies employed persons into major occupational groups: (1) professional and technical workers; (2) managers, officials and proprietors; (3) clerical workers; (4) sales workers; etc. In the past 20 years the total labor force, both male and female, increased about 35 per cent. Meanwhile, professional and technical workers, and clerical workers, as defined by the Census Bureau, showed an over-all gain in numbers of more than 100 per cent.

In contrast, during this same period, sales workers showed one of the smallest gains of any occupational group. In fact, the growth of this group barely kept pace with the increase in the total labor force; there were only 36 per cent more sales workers in 1960 than in 1940. Even more significant is the fact that since 1950—when the postwar boom really took off—the gain in sales workers has amounted to only nine per cent. The picture seems clear enough. Industry has been pushing out products at a tremendous rate during the last 15 years or so, without any great addition to its selling force.

The reasons for this are fairly obvious. U.S. industry, ever since it turned its swords into plowshares with the end of World War II, has been enjoying the fruits of a major spending spree by the hungry American consumer.

Prior to the 1930s, prosperity became a catchword for our economy. But, in point of fact, there were vast unfulfilled demands for products even before 1929. The automobile industry, for example, had yet to reach any sort of maturity in terms of the total population's desire for personal transportation. Few people owned their own homes. Rural electrification was something the New Deal would invent later; even many urban homes weren't wired for the new electrical appliances industry was inventing.

Then came the Great Depression, and prosperity broke down into a decade of underconsumption. Millions remained out of work or were poorly paid in terms of present day standards during the long, hard pull of the 1930s. It wasn't until 1940 when America became, first, the arsenal of democracy, and then a full-fledged participant in World War II, that the U.S. enjoyed full employment. In the next five years Americans more than doubled their liquid savings—from $59.3 billion in 1940 to $136 billion in 1945. What's more, there was an actual decline in outstanding consumer credit—from some $8 billion to about $5 billion. This, of course, reflected the fact that wartime shortages plus a measure of patriotism made it impossible for consumers to spend their savings or incur new debt. They were, instead, building the consumer spending explosion that took place after hostilities ceased and manufacturers

could return to feeding the maw of a public made hungry by depression and war.

In fact, the postwar period marked a great turning point in the history of American capitalism. For the first time, just about anybody could afford the fruits of an organized society's productive capacity. In the 1920s American industry, epitomized by Henry Ford's mass production lines, learned how it could produce great volumes of all sorts of goods. Apparently it took the Great Depression and then a period of redistribution of the wealth, brought about to a great extent by World War II, to teach us how to consume everything industry was able to make.

Distribution revolution

It would be foolish, of course, to say that selling had nothing to do with the consumer boom we have enjoyed up to now. But it certainly wouldn't be foolish to portray that selling effort in terms of a distribution revolution. For one thing, self-service became a great force in the market place. As more and more consumers acquired cars, they became mobile and were willing to travel to buy what they needed. They no longer had to wait for somebody to call on them. Supermarkets and the great chains such as Sears, Roebuck & Co. rapidly latched onto the trend and spread their distribution arms to convenient personal transportation locations.

Certainly such strategy as this can be counted as selling, but it hardly comes under the personal salesmanship category. It amounted to wise marketing planning; merchandise was moved to the suburbs where the market happened to be.

In fact, it became almost smart to see how you could run a business without salesmen; the figures from the Census Bureau bear this out. Customers were ready to buy, and it didn't take that much effort to entice them. They had their savings and their credit and their jobs to back up their pent-up desire for merchandise.

There was more to it than that, though. Advertising came into its own in this lush period. It is difficult to determine whether the sales dollar came before the advertising dollar or the advertising dollar bred the sales dollar. At any rate, both the vast consumer market and the big advertising expenditures grew up together.

Advertising in all forms of media jumped to breath-taking heights after World War II, both absolutely and relatively. In the last year of the war, advertisers spent $2.8 billion —only about 1.6 per cent of personal consumption expenditures. Of course, there weren't so many products to advertise in that year, but the figures matched prewar experience, too.

By 1950 industry was spending $5.7 billion for advertising—2.6 per cent of consumer expenditures. This past year the total advertising bill of $11 billion came to three per cent of consumer expenditures.

Of course, the spectacular growth of television as an advertising medium had something to do with this increase in advertising. There is no doubt that marketers found in TV a brand new way to reach the buying public. Without personal salesmanship—unless you count the Gary Moores and the Arthur Godfreys—companies were able to bring a hard sales pitch for their products and messages right into the living room. As a result, television expenditures jumped from nothing in 1945 to more than $1.5 billion in 1960. Meanwhile, radio and other media such as newspapers and mass magazines also increased their advertising revenue, though not so spectacularly.

Such an explosion of advertising outlays can be analyzed as one more indication that in the great sellers' market of the 1950s U.S. industry was able to move its products by means other than personal selling. Undoubtedly an eager buying public made many choices of products as a result of the blandishments of advertising messages. But, in truth, all an advertiser had to do to move his goods was to make sure his product was easily available—in supermarkets, department stores, roadside discount houses, catalog counters and shopping centers.

It is also probably quite true that, without the new methods of selling and distributing, the postwar boom economy wouldn't have been possible. No such superboom could have relied on the personal selling efforts of a horde of salesmen. The cost alone of maintaining such a sales force would have been prohibitive. Any way you look at it, the personal salesmanship of a bygone day was lost in the consumer boom of the postwar era.

Today the boom has passed, and there is strong evidence to show that the postwar revolution in selling has reached maturity and that there will be a competitive necessity for companies to rethink their marketing strategy to meet a change in the economic climate. It may, indeed, mean a new life for the great American peddler. Perhaps he will be a bit more sophisticated, but nonetheless he will spend his time selling goods to people instead of reading economic charts.

For the next few years, at least, it is certain that the productive capacity of many industries is going to be ample to meet the economy's prospective demand. This means an unrelenting competitive situation in more ways than one. Products will be competing against other brands. They'll be competing against foreign goods. They'll be competing for a consumer dollar which is growing, but which has new and different demands upon it.

Maturing population

Take a look at consumer spending. In 1960, for the first time, the consumer spent over 40 per cent of his disposable income on services. Why? There are a variety of reasons, but they all add up to a maturing population that won't see the likes of the 1950s for some time.

One thing is that families are getting older. The postwar babies are growing into teenagers who require hefty expenditures of a different nature than those required for babies. During the postwar era the young families could stock up on houses, automobiles, major appliances and household furnishings. Today they are spending more for education, leisure time activities and food for growing appetites. In addition, insurance bills are getting bigger and, as schools are built and more teachers are hired, taxes are going up.

Consequently, the manufacturers in the business of selling goods are competing with a myriad of services. Not for some time will new family

formations and a new crop of babies create the kind of automatic market that was enjoyed for so long after World War II.

Thus, companies must make a new attack on their selling problem. Even during the easy days that are past there was evidence that one way to reach and attract the attention of the consumer was through personal salesmanship.

Insurance sales, for example, continued to mount right through the time when people were spending for things they never had before. People wanted protection for new families; also, insurance is looked on as a way to save. In any event it was the insurance salesman, talking to husband and wife in the home, who racked up the big records.

Then there was the amazing success, in a period of stiff competition from self-service stores, of such door-to-door selling companies as Fuller Brush, Avon Products and Stanley Home Products. Electrolux, still considered the leader in vacuum cleaners, never abandoned its door-to-door sales policy. During the latter part of the 1950s, in a time when appliance selling was tough, Electrolux maintained its position—with no cut-rate prices or discount house selling.

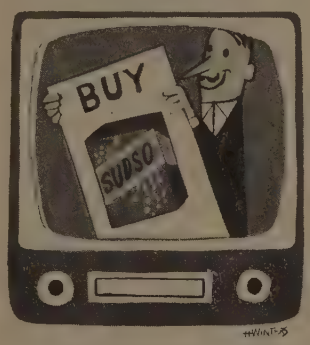
Admittedly such selling can be costly and, for many companies, impossible to maintain. But the lesson is clear: when selling gets tough, customers will still listen to a good sales story if they are properly approached. This doesn't mean that to be successful from now on a company must increase its costs by adding a lot of foot salesmen. But it probably does mean an end to automatic sales.

Readjusted efforts

More and more companies are readjusting their marketing efforts to make sure they get the best use of what salesmen they have. There has been much talk about the marketing concept and the "hard-sell" in recent years. Now those ideas are going to have to be put to work—and that means far more careful day-to-day goal setting and planning at top levels of management. Long-range marketing plans are fine, but they must be translated into daily effort to be effective. Hence, company presidents, many of whom have disdained the rather grubby chore of selling, are going to have to get their hands dirty. This means getting into dreary details—knowing the markets, selling the big customers, seeing that the sales force has a detailed sales plan and the tools to carry it out.

Too many companies are still relying heavily on economic factors or broad marketing plans for their sales effort. In the new competitive economy we have reached, this just isn't going to work. Rather, companies need to discover just what the customers, as individuals and as a class, require. In a real sense, it is the age-old secret of a good peddler: to know what the customer wants better than he knows it himself.

Hence, the job again goes back to



the top levels of management. Strong central planning is needed to devise the tools of selling and to train and inspire the sales force. This is especially true of industrial selling, where impulse buying is almost nil and the proper allocation of salesmen's time is vital to effective and profitable selling. The huge economy we have created is just too big and wide-ranging for personal salesmanship alone. That form of selling will become increasingly necessary, but it has to be backed up with central planning, down to minute details of daily calls. It is the marketing concept, with a peddler's eye view.

Larger picture

None of this means that advertising, promotion and other indirect sales methods will be superceded. They will merely take their proper role in a larger picture of total selling effort.

International Business Machines, for example, in a study of its selling methods, found that more, rather than less, advertising was needed at certain points in its distribution plan. IBM has always relied heavily on personal sales calls by a highly trained and well-paid staff of technical salesmen as the backbone of its marketing. But a research project, dealing with potential banking customers for data processing equipment, revealed that advertising could reduce the direct selling effort substantially in the early stages of making customers aware of their products. Thus, IBM found it could free some of the salesmen's time to allow them to perform where they are most effective—clinching the final order.

Again, this shows that our giant economy requires from the companies which operate in it a sophistication and refinement of marketing practices which no amount of one-man selling can replace. But this doesn't mean that any level of the distribution route can be skipped if consumer attention and interest is to be won. If possible, personal attention to individual customers is necessary as a part of an over-all marketing scene.

Today it is more important than ever for a business to provide something for everybody who handles its product as it moves toward the final market place. This naturally means having a sales staff equipped to do more than take orders. That staff must be backed by solid research, specific instructions and well-defined goals.

Management in many companies today came of age and into power during a time when salesmanship had lost its glamour. Progression to top jobs came through comfortable staff jobs far removed from the wheeling and dealing of the market place. That now must change. There are no magic formulas left for paperwork marketers to devise in an economy where customers more and more are demanding close attention to their problems.

Footwork, perhaps of a different nature than that used by the old-fashioned drummer, is now called for to supplement all the modern methods of communications on which companies relied during most of the postwar period. ■

An aspect of national goals

The Arts in American Life

by AUGUST HECKSCHER

■ THE UNITED STATES has pioneered in the development of an industrial society, with wealth and leisure broadly distributed and a rising standard of living for all. It is committed to material progress; but it has intended that this be accompanied by spiritual and intellectual ferment and a deepening appreciation of the arts. As a people we face the question today whether our cultural standards can indeed be brought into balance with our physical well-being.

Despite outstanding achievements by individual Americans, and signs of broad public interest in the arts, there is cause for serious uneasiness. An industrial civilization, brought to the highest point of development, has still to prove that it can nourish and sustain a rich cultural life. In the case of the United States, it is evident that cultural attainments have not kept pace with improvements in other fields. As the incomes of the people have risen, a proportionate share has not been devoted to intellectual and artistic pursuits. As leisure has increased, so has the amount of time given to unproductive and often aimless activities. Many of these leisure time activities may properly be called recreational; too few can be judged to hold real meaning in the lives of individuals or of the community. . . .

The state of the arts in a society may be judged by the beauty of its public monuments, the scale and fitness and ease of human contacts provided by the squares and streets of its cities, the pleasantness of its country landscape. A people caring about dignity and excellence in their private lives may be expected to care also about the embodiment of these qualities in the public environment.

Excerpted from August Heckscher's contribution to the Report of the President's Commission on National Goals, published in 1960 by Prentice-Hall under the title *Goals for Americans*. Mr. Heckscher's chapter is entitled "The Quality of American Culture."

The American scene today is not reassuring in this regard.

The earlier American achievements in community building, such as the New England town, have been overrun and rendered obsolete by the automobile. The newer cities have been allowed to take form without concern for the human values they should be expected to serve. The countryside, meanwhile, has been left as the prey of the bulldozer, the billboard and indiscriminate commercial exploitation. All this, it must be noted, has been occurring in a society which is lacking in no material boon and has perhaps a higher standard of well-being for the private citizen than any civilization in history. . . .

Democracy conceives of the whole pattern of existence as being unfolded from within. To the extent that the democratic process is not distorted by plebiscites or the manipulation of public opinion, it finds the people not merely consenting to legislative enactments but generating the forces and impulses from which legislation—and indeed every common purpose and aspiration—is born. The image of such a society is not laid up in Heaven. It is being made and constantly remade by the myriad choices and decisions of the citizenry.

If this is true of the laws, it is certainly true of the arts in a democracy. The cultural life of a free people must be sought out. It cannot be decreed. It can be encouraged, guided, sustained. It cannot be imposed from above nor created by will or rational desire. For this reason goals in the cultural field must have a different scope from those that can be set elsewhere. In part the goals must consist of a sensitive appreciation of what is going on in the depth of society, a capacity for awareness, a gift for distinguishing between true and spurious forms of art. At their most ambitious these goals must consist of efforts to encourage and bring to fulfillment the best of what already exists in embryo. . . .

The United States today has its own school of painters, sculptors and architects. It is producing significant results in the performing arts. No one in this generation is likely to ask, who reads an American book? or, who looks at an American painting? Critics in this country and abroad acknowledge a high degree of original creative genius. Its museums and private collections show the foremost art of all centuries, and this is the object of the widest public interest and appreciation. The great books are sold in inexpensive editions to very large numbers. In music the classic compositions have an immense and continuous hearing; and the most famous works of the drama (particularly Shakespeare's) are kept alive for a broad audience.

Fine art is thus being created and enjoyed, both in the form of new works and of the classics of former times. To keep the creative sources in our society open and productive must be a prime objective. In a world where ideology and the interests of the state seek in so many cases to control art and bend it to

particular ends, the freedom of the American artist needs to be noted. At the same time we need to be constantly on guard against those who seek to judge or limit this freedom either because of ideological significance or the political affiliations of the artist.

In a more positive way, the artist must be encouraged and his work supported. It is being gradually recognized in this country that the teacher is entitled to a wage proportionate to the importance and dignity of the work he performs. The same fact must come to be recognized in regard to the artist. At bottom the problem is one of a changed attitude—a change which must begin with a different evaluation of the artist himself. Americans have been accused of being "anti-intellectual"; in regard to art the charge could be even more grave: that they are not so much against it as indifferent to it. The artist has been allowed to make his way in a kind of freedom which has too often been bare and unprofitable because it was not part of an atmosphere of understanding. . . .

Mass society

Disinterested and considerate help for the artist is particularly necessary because of the mass nature of our society. The innovator too far in advance of his times or too independent of current trends and fashions is likely to find the great audience unwilling to listen. The performer who does get the ear of this audience, moreover, is subject to subtle temptations and pressures to compromise the quality of his work. The existence of the popular arts in their present persuasive and insatiable forms provides, indeed, one of the obstacles to the highest development of the fine arts. The need is to make possible fruitful interaction between the artist and the mass audience, but at the same time to give the artist the means of keeping a life somewhat apart, under conditions allowing him to develop in his own way and at his own pace. . . .

Art is the creation of individuals; but in many of its forms it involves individuals working together. By its life it gives life to institutions. The quality of art in a society will in large part depend upon the number, the vitality and the continuity of the institutions of art in its midst.

America has traditionally been rich in institutions. Its people have come together naturally to form committees; from committees have grown organizations. Many of these have been temporary or deciduous, disappearing and reforming as purposes changed or interests shifted. In its cultural life there are examples not only of those vigorous shoots which embody a passing ideal or an aspiration, but of more lordly institutions, solidly rooted in the community, which make their own traditions and evoke established sources of support.

Insofar as art is embodied and carried forward within institutions, the money which goes to these should be on a scale commensurate with the significance of the work. Though support has come from many sources in the past, it has usually come haphazardly, even apologetically, as if society were ashamed of having to sustain these indigent institutions. But the institutions of art cannot by their very nature be expected to exist without aid; making funds available to permit their fullest flowering should be an act of highest satisfaction on the part of individuals and the community as a whole.

Membership drives and admission fees may provide a significant proportion of running expenses; but there are dangers in being too dependent upon these. Museums, as well as other cultural institutions, must be constantly on guard against a deterioration of standards resulting from an appeal to what is immediately popular or even sensational. The pressure to derive fees from the public may have serious effects upon the basic purposes of the institutions. It is essential, therefore, that the community as a whole recognize on a stable and continuing basis its obligation to help meet annual expenses and in exceptional cases to build up endowment funds.

Spotty and uncertain

The sources of community support have been various. Individuals and foundations have found art an appealing form of benefaction. In 21 cities in the United States there have been established "United Art Funds," comparable to the Community Chests, which make their gifts to the cultural institutions of the community. Yet the support has been spotty, uncertain and inadequate. The major source of subsidy still comes too often from the artist himself—from the musician, for example, whose salary is so far below a living wage that he is compelled to take two or even three jobs to supplement it. . . .

The corporation, which has come to the point where it feels fully justified in making contributions to education, must make the further step of contributing as generously—and on as rapidly growing a scale—to the institutions of art. The foundations, some notable exceptions notwithstanding, have neglected this field. A recent authoritative estimate put at only five per cent the amount of total foundation grants going to liberal arts—and much of this is for education, not the creative arts. The community foundations, which represent a growing force, should find the cultural institutions of the community a field as appropriate for their support as hospitals or scholarships. . . .

The lack of [cultural] institutions imposes a fatal handicap on the meeting of artistic needs. A few pioneering, imaginative programs may be successfully undertaken by foundations. The commissioning of works of art and the making of grants to individuals can within limits be carried out. But the steady flow of economic support depends upon channels already having been prepared and creative achievements having found embodiment in durable institutions.

The handicap caused by lack of institutions is especially serious in

regard to the performing arts. With the exception of a few opera and ballet companies, there have been virtually no continuing groups. There is no national theater, and there are only three or four cities with repertory companies. When the United States, following the example of virtually every other Western country, has wanted to send an acting group abroad, it has been compelled hastily to organize and train a band of actors, prepared to give a small selection of plays.

The lack of repertory companies has not only denied the theater the kind of economic support which has gone to other artistic institutions; it has at the same time kept the theater from reaching its fullest development as a medium of culture. Without stable theatrical institutions it is difficult to train actors in the discipline of their art or to give them the varied experience which evokes their full gifts. It has been impossible, also, to create theater which draws upon the range of great and varied plays in the collection of ancient and modern writers. . . .

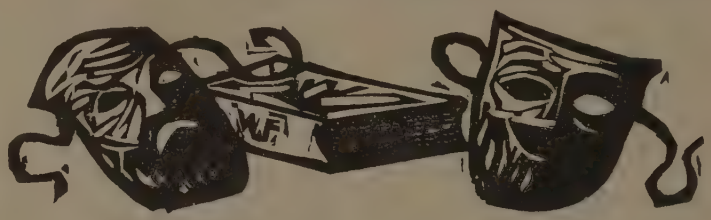
At the root of all this is the fact that theater in the United States has been thought of, not as an art form, but almost exclusively as commercial entertainment. Television confirms this outlook, as the theater talent is increasingly drawn into the orbit of entertainment at the level of the mass audience. Yet the theater remains important to all the arts and to the whole quality of American life. Perhaps no other medium can so effectively bring home to men and women the essential paradoxes of their existence, confronting them with the tragedy and the comedy everlastingly at the heart of things.

Important goal

It seems highly important, therefore, that the objective of creating repertory theaters in the United States, situated in the larger cities, perhaps related to the universities, should be a recognized goal. This should be accompanied by a determination to see that funds from various public and private sources flow to the theaters as to the other institutions of art. In addition there exists a large scope for imaginative experiment, on the part of foundations and other institutions, with the purpose of giving young actors, playwrights and scene designers opportunities for developing their gifts.

The role of government in the arts has been a matter of much controversy—and of considerable obfuscation, not least among those who themselves represent the cause of the arts. It seems necessary to speak plainly on this subject. . . .

Where government has entered directly into the field of art, the experience has almost always been disheartening. Political influences have exerted themselves; the standards of the artist and the critic have been ignored. Where these have been permitted a measure of authority, the tendency has been for an artistic clique to entrench itself. The art which has been encouraged under official auspices has almost always favored the less adventurous and the more classically hidebound schools.



Sophisticated standards

From this experience leading figures in the art world have drawn the conclusion that anything is better than the intrusion of government. It may be questioned, however, whether such men are not thinking too narrowly as professionals, without an adequate understanding of the governmental methods and institutions which in other fields, no less delicate than art, have permitted the political system to act with detachment and a regard for the highest and most sophisticated standards.

The judiciary itself is an invention of tremendous ingenuity, permitting laws to be administered independently of political pressure. The functions performed by the Central Intelligence Agency or the Federal Reserve Board are, to take two modern examples, quite as complex as the encouragement of art; they are performed with a high level of competence and professional skill. Certainly in the United States of the next decades we should be capable of devoting as much ingenuity to the creation of adequate processes for the nurturing of art as we have for regulating the interest rate or pursuing the cold war. . . .

What, then, should the government do in this field? It should consider, first of all, undertaking a number of relatively undramatic and indirect measures. . . . What is important is that leaders within our society—private citizens and public officials, scientists, curators, educators, artists—should all agree that government must not thwart, and wherever possible must positively encourage, the development of the cultural life. Such agreement has been lacking, and as a result nobody has fully envisaged the scope and diversity of the action which might be taken.

Our tax laws could be combed over with the question in mind of where they could be adjusted so as to make the pursuit of cultural attainments easier. Taxes which now burden the theater and music should be removed. Tariff laws should be looked at from the point of view of art and cultural exchange. In virtually every department of the federal government there are activities touching the arts which should be coordinated and vitalized. . . .

Useful role

A proposal for the establishment of a Federal Advisory Commission on Art has been before the Congress. It should certainly be passed. Provided this were composed of men and women who are really concerned with the issues involved, the Commission could perform a genuinely useful role in making studies of the whole field of arts in relation to government. There exist ample

possibilities for creative innovations. It has been suggested, for example, that a subsidy for the transportation of art could help greatly in bringing it on a larger scale to the citizens.

Grants and subsidies

It has been suggested that a tax on television might be used in the form of grants and subsidies to encourage those sources of art and talent from which television derives its sustenance. These measures, and many others, should be looked at with an open mind; they should be related to what is being done in other countries for art and to what is in accord with our traditional methods and habits.

In the main, government can be active insofar as the institutions of art already exist in the community. A local government could do actual harm in constructing a theater where no repertory company exists or where a responsive audience is not in being. But where there are healthy institutions government can lend its support as naturally to a museum as to a library, to a ballet corps as to a school. It can provide, or help provide, the permanent facilities within which art is performed. A city government without too much soul-searching will build a baseball stadium or a fair grounds. Is it unreasonable to ask, where there is a clear demand and sound institutions, that it provide a home for the opera or theater company?

In the nature of things government cannot create art. That is no reason why it should not create a home for art—a feat which it is admirably qualified to perform. Nevertheless, the Congressional action which provided for a National Cultural Center allowed that no funds be provided for the building. It is admirable that there should be plans to raise the money from individual, foundation and corporation sources; but the very fact that such activity is afoot should persuade the government of a positive duty in this field. The national government should certainly have a hand in the National Cultural Center, just as it did in building the National Gallery of Art. It may be pointed out, incidentally, that the government, which feels restrained from building a cultural center in Washington, did not hesitate to build an extremely handsome one for the people of West Berlin. (In the latter case it kept its principles pure by action under the cover of a specifically created "foundation. . . .")

The support of going institutions of the arts and culture is something which government can and should do at every level. Municipal support is a well-established principle, with amounts ranging from $5 million annually in New York City, a little under $1 million in Philadelphia, down to $1,600 for the city of Washington. The programs supported are mainly museums and orchestras, although Houston provides a small sum for the repertory theater. Support of the arts at the state level has been more spotty, with activity mainly confined to the appointment of commissions concerned with public buildings. But the concern of the states is increasing, and ought to increase markedly over the next decade. The entrance of the federal government into this sphere (apart from its concern for the District of Columbia) would present new problems as well as new opportunities. There is no reason why this should not be done, but the principle ought definitely to be established of having the federal government give grants to state institutions only on a matching basis.

Great exemplar

Apart from activities in support of the institutions of art, government is itself the great exemplar in this as in other fields. It creates standards and sets style in the course of pursuing its basic objectives. This is true of government at all levels, but particularly so of the national government. Washington has been involved in one way or another with the arts since its founding. It has been the great builder, the great coiner, the great printer and collector of books, and inevitably the repository of great works of art. The question today is not whether the government shall do these things, but whether it shall do them well or ill.

Government's obligation is, in brief, to keep its own house with a sense of beauty and fitness. In doing this, as in supporting art in different ways and at different levels of the national life, government should be entirely clear about its own purposes. It is not seeking to increase employment among impoverished artists. It is not conducting a welfare program for deprived citizens, nor trying to win the cold war by showing that we have more and better art than rival regimes. It is seeking to encourage art for its own sake as an expression of what is noblest in the people's lives; it is seeking to create for the public the finest objects to which our culture can attain.

Significant goal

The most significant goal in the field of the arts is that their enhancement and development should be considered a goal—that the American people should recognize the objectives in this area of their common life to be on an equal with those which in the past they have given their best efforts. It has been all too natural, during epochs when a continent was being subdued or amid the fresh responsibilities of world power, to think of the arts as something pleasant but peripheral. The time has now come when we must acknowledge them to be central and conceive their fullest development as essential to the nation's moral well-being.

This country is being watched by peoples—many of them as new to nationhood as they are old in cultural achievements—who ask whether under such a system as ours the highest values can be maintained. It is being watched—and judged. Among our own people, meanwhile, there is a deep and persistent questioning about the significance of our material advance. The ultimate dedication to our way of life will be won not on the basis of economic satisfactions alone, but on the basis of an inward quality and an ideal. Among much that on the surface appears to be complacency or materialism, the Americans—the younger generation especially—are looking for something at once more demanding and more genuinely satisfying than what passes for happiness by current standards. To minimize or frustrate this quest is to risk weakening the fabric of our whole society. ■

The Spenders. Steuart Henderson Britt. 293 pp. New York: McGraw-Hill Book Co., Inc. $4.95.

• Dr. Britt, Professor of Marketing and Advertising at Northwestern University, has written a book that can be read as a rebuttal to Vance Packard's condemnation of "consumerism" (consumption for the sake of consumption) in *The Waste Makers.* In fact, these two books make excellent companion pieces. Not only do they present the opposite sides of a controversial issue, but they are strikingly similar in style; both are quite facile and filled with repetitious, often unnecessary, quotes, cliches and examples.

As the publisher's jacket states, Dr. Britt's book is meant to "destroy the myth that American business encourages reckless consumer spending." The author is convinced that the consumer is indeed "king" in our society and that the functions of advertising, brand names, packaging, motivation research, etc., are grossly misunderstood. They are not insidious "hidden persuaders" aimed at bamboozling the consumer; rather they are the means through which the consumer "king" can be better served.

There is undoubtedly much to be said in favor of this thesis, but the reader does get the impression that Dr. Britt is, himself, carrying on an advertising campaign rather than writing an impartial analysis of a genuine problem.

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Problems of American Economic Growth. Bruce R. Morris. 279 pp. New York: Oxford University Press. $2.50.

• The author of this book, who teaches economics at the University of Massachusetts, examines the factors that affect economic growth, such as raw materials, population, capital, technological change, entrepreneurship, consumer demands and government expenditure. He identifies bottlenecks that might impede growth—for instance, deficiencies in education, the lack of enough pure scientists and a shortage of an adequate water supply.

Morris points out areas in which our knowledge is lacking, such as how to attain balanced economic growth. He lists the vital problems that need to be solved. Among them are: the promotion of education, both of the general public and of experts; the determination of the "right" distribution of income for growth; and the settlement of the relative power of groups such as business, labor, farmers, consumers and the government.

Finally, Morris reminds the reader that economic growth is only one of a people's objectives and that we must decide what it is that we want and the place of economic growth in our desires. Until we have done this we cannot draw up a policy for attaining our objectives.

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The Export Economies. Jonathan V. Levin. 347 pp. Cambridge, Mass.: Harvard University Press. $6.75.

• Westerners moved into Asia, Latin America and Africa largely to develop and export raw materials—minerals and agricultural products. Levin examines why this development did so little to benefit the people who lived in these lands. The "export economies" of such countries were often superimposed on a subsistence economy. Capital was supplied by the West, labor was frequently imported and the export sector of the economy often had little effect on the rest of the country. A very large share of the income generated by the exports was remitted abroad as interest, savings by foreign personnel and in payment for consumer goods. And the export economies rarely created a large enough local market for much industry to develop.

Today, however, the picture is changing. Newly independent lands and those approaching independence have introduced measures to retain within the country a far larger share of the income from exports. In many cases this money is used for economic development. Levin examines how this income is diverted and shows how this has often meant that governments assumed economic functions, such as operating marketing boards or taking over mines and plantations. He warns that the pressure on foreign interests may, in some cases, destroy the export business and impoverish the country.

Levin has produced a valuable economic study of some of the major problems facing underdeveloped nations. It is, unfortunately, marred for the general reader by excessive repetition and a dull, technical style.

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Social Change in Latin America Today. Richard Adams, *et al.* 353 pp. New York: Harper & Brothers. $5.00.

• Under the auspices of the Council on Foreign Relations, six leading students of Latin America have analyzed the social forces that are reshaping the societies of Latin America and have highlighted their meaning for American policy.

A general introduction by Dr. John P. Gillin, Dean of Social Sciences at the University of Pittsburgh, discusses how race, economics and values in Latin America have produced an emerging middle class that differs markedly from the middle classes of Western Europe and North America. Succeeding essays discuss in more detail five specific areas—Peru, Bolivia, Brazil, Guatemala and Mexico.

The book, as a whole, provides a background for understanding the sources of political and social turmoil in Latin America. As such, it outlines the challenge facing the U.S. as we examine and reshape our Latin American policies.

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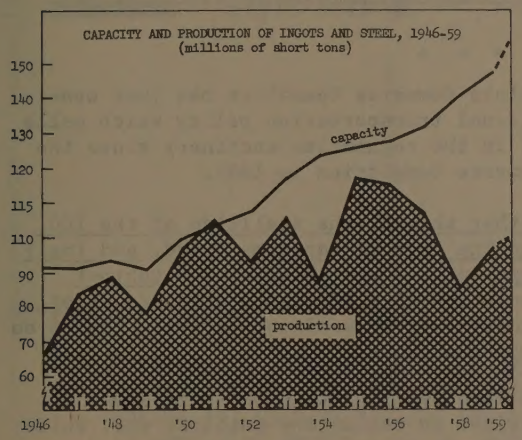
Human Values Where People Work. Thomas G. Spates. 246 pp. New York: Harper and Brothers. $4.50.

• As the title implies, the author is primarily concerned with the "human values" in the job environment as opposed to the material ones of wages and fringe benefits. After devoting the first 47 pages to short sketches of business and labor leaders whom he regards as "pioneers" in emphasizing human values, Prof. Spates embarks on a pedestrian discussion of the moral precepts which underlie these human values. He believes that modern personnel administration should be based on the moral principles enunciated in such milestones in the history of man as the Ten Commandments, the Sermon on the Mount, the Declaration of Independence and the Atlantic Charter. While it is hard to oppose the author's appeal for more concern with human values where people work, this volume sheds no new light on the problem.

THE DOMESTIC ECONOMY—All is not well with the steel industry. Steel production has declined by more than 13% from its 1955 peak of 117 million ingot tons—in spite of a 12% rise in real gross national product. For the last 6 months more than half of the industry's steel-producing capacity has been idle.

In a sense the steel industry's problems seem a good deal more serious than they really are. Thus the 13% decline in production between 1955 and 1960 was matched by only a 2% decline in domestic steel consumption. Part of the reason for this has been a marked swing from inventory accumulation to inventory liquidation—especially during the last year. This will probably be temporary.



The growing competition from foreign steel is more serious. In 1955 we exported 4.2 million tons of finished steel and imported only 1.1 million tons. Last year our exports declined to a little over 3.2 million tons while imports had increased to about the same figure—a loss of 3.1 million tons of finished steel, or 4.4 million tons of ingot production. The revival of European steelmaking capacity chiefly explains this shift which will continue in the immediate future.

But the real problem facing the industry is that the demand for steel has remained virtually unchanged while the rest of the economy has expanded.

Thus more than 2/3 of the decline in steel production during the last 5 years is attributable to a decline in steel's 3 traditional customers—autos, construction and maintenance, and ordnance—who together buy about 1/4 of the output.

> The auto industry, which uses 22% of total steel output, has reduced its annual consumption of steel by more than 1/5 between 1955 and 1960, partly as a result of lagging sales and partly because the compact models use less steel. Consumption of steel by the construction and maintenance industry has remained virtually unchanged during the last 5 years in spite of the phenomenal construction boom. Steel's third most important customer, ordnance (which includes military equipment), has reduced its consumption of steel by more than 3.2 million net tons since the end of the Korean war in 1953.

Some of these losses will undoubtedly be recouped as traditional markets expand and the industry finds new ones. But steel will find itself in increasing competition with other materials.

> At present competition from substitute materials is still relatively slight; only an estimated 4% of the total steel market has thus far been captured by substitutes. But this displacement has taken place in high-price and high-profit items, and is more serious than aggregate statistics would indicate.

The fact of the matter is that customers are becoming increasingly sensitive to price. Between 1947 and 1960 steel prices increased 2.5 times faster than industrial prices. In the past, customers felt compelled to buy no matter what the price. Today they can buy steel overseas and, in some instances, can shop for substitute materials. Indications are that in recent months they have been doing just that.

new Clayton Act test

ECONOMIC NEWS NOTES—The Justice Department has entered a new area in its efforts to enforce the antimonopoly provisions of the Clayton Act. The antitrust division has filed suit in Federal District Court to dissolve the Penn-Olin Chemical Co., a joint company created last year by the Olin Mathieson Chemical Corp. and the Pennsalt Chemicals Corp. The new firm was set up to operate a plant at Calvert City, Ky. to make and sell sodium chlorate.

According to the government, such joint ventures have become a means whereby competitors, "without completely merging, pool their capital or technology to establish a new business entity."

The suit, whose outcome will undoubtedly be decided by the U.S. Supreme Court, is the government's first attempt to prove that a joint company created by 2 competing companies violates Section 7 of the Clayton Act.

* * *

Big changes for the commissions?

The staff of the Senate Interstate Commerce Committee has just concluded a two-year study of national transportation policy which calls for the most sweeping overhaul in the regulation machinery since the creation of the Interstate Commerce Commission in 1887.

The report recommends, among other things, the abolition of the ICC, the Civil Aeronautics Board and the Federal Maritime Board, and their replacement by a Federal Transportation Commission at the Cabinet level. It also calls for the creation of a "Transportation Court of Appeals" whose appellate jurisdiction over decisions of the Commission could only be appealed to the Supreme Court.

These recommendations are even more sweeping than those of James M. Landis, President Kennedy's adviser on regulatory matters, who, while he favors the creation of a new Transportation Commission to coordinate over-all policy, still wants to retain the ICC, CAB and the Maritime Board to exercise day-to-day regulatory functions.

Any sweeping recommendations will probably be resisted by the regulated industries who feel that their individual problems are better understood by a commission which only oversees one industry rather than by an agency concerned with over-all transportation policy.

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UMW cuts pensions

The recent decision of the United Mine Workers Welfare and Retirement Fund to cut the pensions of retired bituminous coal miners from $100 to $75 per month has made many unions reconsider their methods for financing the pensions of retired workers.

The UMW fund is financed by a 40¢ royalty the mine owners pay on each ton of coal mined. This revenue has declined over the past year because of rapidly declining business in the coal industry.

The experience of the coal industry has reinforced the contention of many unions that the best way to finance a retirement system is for management to make contributions to a fund for the individual worker during his working years rather than tying pensions to the business the company might do in the years after he retires. Pensions based on an output royalty, however, were more popular when these plans were first instituted as the best means of providing pensions for workers about to retire.